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CEO succession processes and agency costs

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CEO SUCCESSION PROCESSES AND AGENCY COSTS

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ABSTRACT

In the ‘passing the baton’ succession process, the incumbent CEO/Chairman relinquishes the CEO title, but retains the Chairman title to facilitate monitoring the new CEO during a probationary period. The new CEO eventually wins the Chairman title if he is successful during the probationary period. We argue that this type of succession process can lead to managerial conformism and conservatism because reputation concerns give the retiring CEO incentives to pressure the new CEO to continue existing policies and to avoid making major changes that could substantially improve performance or increase firm value. Consistent with this hypothesis, we find no changes in operating performance, abnormal stock returns, or the number of policy decisions the new CEO makes during his probationary period, but significant increases in all of these measures after the probationary period ends. Managerial entrenchment exacerbates succession-securing behavior during the probationary period, while effective monitoring and control mitigate it.

CHAPTER 1
INTRODUCTION

Recent corporate events have focused attention on a fundamental question in corporate governance research: How effective are boards of directors in monitoring the activities of CEOs? Determining the costs and benefits of separating the titles of Chief Executive Officer (CEO) and Chairman of the Board is a central issue in answering this question. The Securities Exchange Commission is trying to pass regulations to permanently separate these two titles, while all financial and management media including *Wall Street Journal* and *Harvard Business Review* publish articles on the pros and cons of separate titles. Managerial succession methods, once part of the internal workings of companies have thus become the central topic of discussion in all platforms from classrooms to news rooms. Proponents of dual leadership (i.e., having separate individuals hold the two titles) have argued that unitary leadership (i.e., having one individual hold both titles) amounts to the CEO "grading his own homework". Dual leadership is presumed better because the CEO has an independent monitor in the Chairman.

Brickley, Coles and Jarrell (1997) argue that there are costs to dual leadership and that its benefits are overstated since most firms with dual leadership are simply transitioning to unitary leadership. In this transition process, the incumbent CEO/chairman relinquishes the CEO title to an heir apparent, but retains the chairman title to help monitor the new CEO during a probationary period and pass along relevant information. Good-performing CEOs eventually obtain combined CEO/chairman titles. With the former CEO as Chairman ready to step in if necessary, it is easier to terminate

new CEOs who perform poorly. Vancil (1987) terms this succession process, common in U.S. firms, "passing the baton."

I argue that the common probationary succession process, known as passing-the-baton, can create agency problems stemming from the retiring CEO's incentives. Brickley, Linck and Coles (1999) argue that the prospect of serving on other firms' boards of directors provides a promotion-like incentive for retiring CEOs, and find that the likelihood of obtaining such post-retirement positions depends on the retiring CEO's past performance. To increase the likelihood that outsiders view his past performance positively, a retiring CEO that remains as chairman during a new CEO's probationary period has incentives to encourage his successor to continue his policies and projects. Continuing existing policies and projects makes it appear that those decisions were good even if they were bad ex ante or ex post based on the new CEO's information. The retiring CEO should also have incentives to discourage his successor from making major policy changes that could increase the operating performance and value of the firm substantially because this would signal to outsiders that the retiring CEO's policies did not maximize firm value. We call these incentives by the retiring CEO to make his successor conform "succession-securing behavior". Succession-securing behavior is costly for firms that need to change the retiring CEO's policies to maximize shareholder wealth.

The test-like nature of the succession process, with the retiring CEO as chairman of the board monitoring and evaluating the new CEO's performance, simultaneously provides incentives for the new CEO to curry favor with the old CEO. Since the new CEO understands the incentives the retiring CEO has, he has incentives to maintain the

retiring CEO's policies and projects and to avoid substantial increases in operating performance or firm value as long as the retiring CEO is still chairman.

Agency problems stemming from managerial conformism end when the new CEO obtains both titles and the retired CEO steps down from the chairmanship. Thus, if managerial conformism negatively affects CEO decision-making activity and firm performance, I should observe non-positive changes in these areas while the new CEO is monitored by the retired CEO as Chairman, but improvements in these areas once the probationary period ends. I also expect that managerial conformism to be higher if the departing CEO is entrenched, leading to longer probationary periods. Conversely, external monitoring mechanisms like outside board members and institutional blockholders should reduce the severity of managerial conformism by 'monitoring the monitor', leading to shorter probationary periods with less conformism imposed. Additionally, share ownership by the retiring CEO should decrease succession-securing behavior because his interests are more aligned with those of shareholders.

I test my hypotheses about managerial on a sample of 203 firms that announce probationary-type CEO succession processes between 1993 and 1995. Consistent with the presence of managerial conformism, I find non-positive changes in the number of policy decisions the new CEO makes, operating performance, and abnormal stock returns during the probationary period. In contrast, I find significant increases in these measures after the probationary period ends and the new CEO obtains the combined CEO and chairman title. I find managerial conformism to be exacerbated by increased entrenchment of the departing CEO. The longer the tenure of the departing CEO is in the firm, the higher the likelihood and costs of managerial conformism. On the other hand,

efficient external controlling by institutional blockholders or outside board members reduces managerial conformism problems. Larger and older firms, who are easier to monitor have less managerial conformism problems, while younger and smaller firms have more managerial conformism. Larger firms with better external controls can even use probationary succession processes to their benefit.

My results shed new light on the agency costs of a common succession process. Collectively, the extant literature produces ambiguous conclusions about the superiority of unitary versus dual leadership. Since the passing-the-baton process involves temporary dual leadership, my evidence of managerial conformism suggests another cost of the dual leadership structure.

My work is related to Naveen (2003), who documents that the tenure of the heir apparent and the time between the appointment of the heir apparent as COO or President and his subsequent appointment as CEO are longer in firms with passing-the-baton-type succession processes. She also finds abnormal returns at the announcement of CEO turnover to be lower for firms with relay-type planned succession processes. Naveen concludes that these results imply greater information transfer needs. Her results are also consistent, however, with the type of managerial conformism I document in this dissertation.

Chapter 2 provides a detailed literature review, and chapter 3 develops the hypotheses to be tested in this dissertation. The data and methodology are detailed in chapter 4. Chapter 5 provides a detailed description of the various CEO succession processes in the U.S. The univariate test and regression results are provided in chapters 6 and 7, respectively. Chapter 8 concludes the dissertation.

CHAPTER 2
BACKGROUND AND REVIEW OF EXISTING LITERATURE

According to the definition in textbooks, corporate boards provide a link between the providers of the capital (shareholders) and the people who use that capital to create value (managers). Therefore, their main function is to monitor the actions of the management on behalf of the shareholders. However, in 93% of the largest U.S. companies, the chief executive officer is also the chairman of the board of directors (Monks and Minow, 2001). This inherent conflict has attracted significant attention from both the financial media and the academic world. A 1992 National Association of Corporate Directors (NACD) survey of corporate directors states that 20% of corporate directors believe that separating the CEO and chairman positions would have a positive effect on boardroom performance. Similarly, 20% of the directors surveyed believe that such a separation will have a negative effect. The remaining 60% think that the impact of separating the roles would be neutral (Monks and Minow, 2001).

In this dissertation, I define dual leadership as having two separate individuals hold the CEO and chairman of the board titles, in other words, as the firm having dual leaders. Unitary leadership on the other hand, refers to a single individual holding the combined "CEO and Chairman of the Board" title.

2.1. Benefits and Costs of Dual v.s. Unitary Leadership

Proponents of dual leadership base their arguments on the claim that combining the titles of CEO and chairman of the board results in the CEO grading his own homework[1] (Brickley, Coles and Jarrell, 1997) and thus increasing managerial discretion

[1] As Brickley Coles and Jarrell (1997) also note, this schoolwork reference is attributable to Blenyth Jenkins, the director of Corporate Affairs for a London based trade group, who was quoted in the below

while decreasing the monitoring efficiency of the board of directors. In other words, separating the roles of CEO and chairman leads to a more objective evaluation of the CEO and creates an environment for greater accountability. In the post-Enron financial environment, this argument finds more spotlight with the SEC trying to enforce tougher corporate-governance standards, and the financial media like the *Wall Street Journal*[2] advocating separation of combined CEO/chairman titles.

Fama and Jensen (1983) argue that agency costs can be reduced by institutional arrangements that separate decision management from decision control. These terms respectively refer to the right to initiate and implement resource allocation decisions and the right to ratify and monitor the implementation of these decisions. Thus, dual leadership, with a separate CEO and a chairman, is a means to achieve such institutional decision control mechanisms.

Though scant and mixed, there is some empirical evidence showing that separating the titles of CEO and chairman of the board improves firm performance. Pi and Timme (1993) examine a sample of 112 banks, 25% of which have dual leadership, over the 1987 – 1990 period. After controlling for firm size and other relevant variables, they find evidence that costs are lower and return on assets is higher for firms with separate CEO and chairman titles. Similarly, Rechner and Dalton (1991) examining the differential financial implications of dual/unitary leadership decisions for 141 corporations over a six-year time period, find that firms opting for dual leadership

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cited New York Times article as follows: "One of the major functions of the board is to supervise management. If the Chairman of the Board is also in management, then he is in effect making his own exam papers." ("Balancing the power at the top. British Style" by Richard Stevenson, *New York Times*, Sunday, November 15, 1992)

[2] See, for example, "Splitting posts of Chairman, CEO catches on" by John S. Lubin, *Wall Street Journal*, November 11, 2001, page B-1.)

consistently outperform the firms with unitary leadership. Baliga, Moyer and Rao (1996), analyze 181 industrial companies over the 1986-1991 period, and find some evidence that leadership structure matters: that firms that switch to dual leadership have better long-term performance than firms that maintain unitary combined leadership. This evidence is weak, however, and since they fail to find significant changes in market value or operating performance around changes in duality status, the authors conclude overall that there is little evidence to support the hypothesis that dual leadership leads to better firm performance.

Brickley, Coles and Jarrell (1997) challenge this evidence, and find that while about 14% of the firms have separate titles, most of these firms are simply transitioning to new CEOs, where good performing CEOs are eventually granted both titles. Thus, the frequency of separate titles and the tests associated with it are potentially overstating the evidence.

Most opponents of dual leadership base their arguments on the costs of having two heads. They believe that a board of directors will be run more efficiently and less costly with combined CEO/chairman positions. Brickley, Coles and Jarrell (1997) also specify these costs associated with dual leadership:

- Agency costs of monitoring the non-CEO chairman. In the spirit of Alchian and Demsetz (1972), 'who monitors the monitor?', the shareholders will now have to incur the additional cost of monitoring the chairman and making sure he acts in their best interests.

- The information costs associated with the costly and incomplete transfer of the critical strategic information between the CEO and the chairman. Information transfer will be costly between the CEO and the chairman.
- The actual costs of the CEO succession process itself within the company.
- The confusion of having two leaders of the company.

2.2. Probationary (Relay-Type) Succession Processes

Vancil (1987) names the common succession process in U.S. companies as "passing the baton." In this process,[3] where the incumbent/former CEO, who has recently relinquished the CEO title to the heir apparent[4], or – passed the baton, – retains the title of chairman of the board during a probationary period in order to allow the board to better monitor the new CEO in action as well as pass down any relevant information to the new CEO. In essence, the former CEO, helps the Board put his successor to a test and if or when the new CEO passes this test, he is awarded with the combined title of CEO/chairman while the former chairman steps off the Board. Vancil (1987) also argues that this transition period during which the CEO and chairman titles are separate is structured to readily oust the new CEO in case he "drops the baton," or fails the test.

Brickley, Coles and Jarrell (1997) test Vancil's (1987) passing-the-baton hypothesis indirectly and find that dual leadership firms have younger CEOs with shorter tenure, who own less stock and receive lower compensation levels with respect to combined CEO/chairman of the firms in their sample with unitary leadership structures. Also, most of the separate chairmen in their sample are former CEOs or people with

[3] Most of the relay race analogies are originated in Vancil's 1987 book, *Passing the Baton: Managing the Process of CEO Succession*, but have continued into the literature. Brickley, Coles and Jarrell (1997) and Naveen (2003) also use the same terminology.

[4] The heir apparent, in most cases, is the chief operating officer (COO) or the president of the company, and the new CEO in the first couple of years of his tenure usually carries such an operating title as well.

detailed knowledge of the company and relatively high stock ownership, and that the titles are separated only when the information and agency costs of dual leadership are low. Thus, they conclude that separating the titles of CEO and chairman of the board is usually a part of the succession process of CEOs. In other words, passing-the-baton is a prevalent strategy and the main reason for the existence of dual leadership in most firms.

Additionally, in contrast to the previous empirical studies, Brickley, Coles and Jarrell (1997) find no evidence that unitary leadership structures lead to inferior accounting or market returns. They find instead that changes in leadership structures have no systematic effects on stock prices. If anything, their findings suggest that dual leadership is associated with systematically lower cash flows and value.

Naveen (2003) analyzes the factors that influence the choice of succession plans and finds that firms that are more human capital specific and firms that operate in more heterogeneous industries are more likely to have planned succession processes and are more likely to choose inside successors. Moreover, she finds succession planning to be more likely in larger and more diversified firms.

2.3. Probationary (Relay-Type) Succession Processes and Agency Costs

One aspect of the probationary succession process that is not thoroughly examined previously is the phasing out of the former CEO, and the incentives associated with this process. Vancil (1987) discusses the emotional burden on the incumbent CEO of stepping out and identifies it as an exit barrier that needs to be mitigated by some prospect of emotional satisfaction after stepping down. First, Vancil (1987) argues that the CEO might be reluctant to give up the perquisites that come with the CEO office. Also, the status of the office entitles the CEO to a very select peer group with a broad set

of useful contacts. Most importantly, unless the CEO has already started planning for retirement, stepping down presents the prospect of being unemployed and not having something to do.

Similarly, Brickley, Linck and Coles (1999) argue that while prospects for promotion provide incentives to lower-level managers in the U.S. and in Japan, promotion incentives do not exist for top managers. The only mechanism that might provide promotion-like incentives is the prospect of being retained on the board of directors after retirement. Yet, these incentives can only exist if the retention decision is based on the top manager's performance during active employment. Their results suggest a positive and statistically significant relation between post-retirement board service and performance for retiring managers in both countries. They find that retention on the CEO's own board depends primarily on stock returns, while service on outside boards is better explained by accounting returns. Thus, top managers' career concerns do not necessarily end at retirement.

Thus, the former CEO in a probationary succession process has incentives to encourage his successor to follow in his footsteps and continue the projects he has worked hard to prosper, signaling that the investments, policies and decisions made during his time are profitable. Simultaneously he would discourage his successor from making major policy changes that would imply poor management on his part. In other words, the retiring CEO still has his reputational capital at stake upon becoming the chairman of the board of directors. These may lead the former CEO to be more reluctant in passing down relevant information, thus increasing information costs mentioned by Brickley, Coles and Jarrell (1997). Similarly, they may lead the chairman into trying to

block some of the decisions of the new CEO by lobbying against him in the board, and thus increasing agency costs. On the other hand, even if the former CEO does not perceive his reputation at stake, he is very likely to believe in the real merit of his policies and decisions, and thus try to make sure his successor follows and even improves upon them, naively believing that it is in the best interests of the company. Consequently, a passing-the-baton type of succession plan may provide healthy companies that are managed well with a smooth and efficient succession. Simultaneously, they might be very hazardous to companies that are not healthy, and need fundamental changes.

Furthermore, successful implementation of policies requires a good understanding of and extensive experience with the specific production technologies of the firm and its product markets. Most executives, in addition to having worked for the firm, may have invested in assets that they believe to be more valuable under their management than under the management of others (Schleifer and Vishny, 1989). This would increase the probability of managerial conformism behavior and increase the agency costs of a passing-the-baton type succession process (Parrino, 1997).

Monks and Minow (2001) note that in 27% of the S&P 500 companies, a former CEO remains as a board member, and six companies even have two former CEOs serving on their board.[5] Monks and Minow (2001) portray the problems related to the retired CEO serving on the board of his own company as a Catch-22 for the retired CEO: "The retired CEO that cares about his successor will not be an objective and effective director. On the other hand, retired CEOs that want to dominate the board should not be on the board in the first place."

[5] Monks and Minow (2001) obtain these numbers from a 1991 Institutional Shareholder Services, a consulting firm that advises investors on corporate governance issues, survey of S&P 500 firms.

Vancil (1987) presents an example of how CEOs will sometimes do everything in their power to make sure their successor keeps their policies and dreams alive. For instance, he notes that Ben Branch, the CEO of Dow Chemicals from 1971 to 1976 enhanced the presence of Dow Chemicals in Europe, made Dow Europe powerful and the center of corporate policy and the hallmark of his own career. Therefore, when he decided to step down from the CEO position a couple of months early, he influenced the board to vote for the then-president of Dow Europe, a European himself, Zoltan Merszei, as his successor, in spite of all the management team's reluctance to do so. During the two years, he stayed as chairman of the board after that, Branch tried to make sure the European growth project took the topmost priority in the firm's agenda, and Merszei stayed in position to run it while he discarded the frictions that arose within the top management and the board. Finally, when it became obvious that Merszei could not hold the CEO position any longer, Ben Branch himself had to resign from the chairman position to allow Merszei's resignation from the office of CEO (Vancil, 1987). This example also illustrates how passing-the-baton type succession process can trigger the ousting of a new CEO that fails to the test or "drops the baton".

The resemblance of the succession plan to a test gives the former CEO, the current chairman, the incentives and the power to exert pressure on the new CEO to make him conform to his norms and rules[6]. Vancil (1987) states this problem as:

> "The new CEO may also feel some pain [during the transition period]. He is ready to get on with his own tenure and may feel constrained about

[6] This problem has been named in literature as managerial conformism and succession-securing behavior. Usually, when the new CEO conforms to the status quo, it is named managerial conformism. On the other hand, if the old CEO, somehow enforces conformity, it has been named succession-securing behavior. I have tried to use managerial conformism throughout the text, but both terms have been used interchangeably in the literature, usually based on who the initiator of the conformist behavior tends to be.

> proposing new initiatives or disposing of past mistakes while his predecessor, who is responsible for those sins, is still in the room and practically running the meeting" Vancil (1987).

Sonnenfeld (1988) analyzes the retirement patterns of over 300 CEOs of top U.S. companies with personal interviews, questionnaires and objective data from proxy statements. He argues that the CEO himself makes the decision to stay on the board, and asserts that poorly performing CEOs are among the most likely to stay on the board, because their visions for the company remain unfulfilled.

Naveen (2003) documents that the tenure of the heir apparent, the time between the heir apparent's appointment as COO or president, and his subsequent appointment as CEO, is longer in firms with relay-type succession processes. Similarly, she finds abnormal returns at the announcement of CEO turnover to be lower for firms with relay type planned succession processes. Though she concludes that these results imply greater information transfer needs, she cannot rule out the lengthening effect of managerial entrenchment on the length of heir apparent tenure.

In summary, passing-the-baton style succession processes are used widely by U.S. corporations. The incumbent CEO and chairman of the board initially relinquishes only his CEO title to an heir apparent for a probationary period. During this probationary period, the departing CEO remains as the chairman of the board and serves alongside the incoming CEO. Upon successful completion of this probationary period, the new CEO gets awarded the chairman of the board title as well, and the firm goes back to unitary leadership. While the probationary period in these successions facilitates improved information transfer between the departing and incoming executives and a closer

monitoring of the new executive while he gets acclimated, it may also create agency costs for the firm. The departing chairmen have incentives to make sure their successor conforms to their goals and standards. Though such managerial conformism may be beneficial for healthy and stable firms by maintaining the high standards, it may be detrimental for firms that are in need of managerial change. The following chapter develops and states specific hypotheses about how such managerial conformism would affect firms as well as the factors that determine the level of managerial conformism in relay-race type probationary succession processes.

CHAPTER 3
HYPOTHESES AND PREDICTIONS

This chapter of my dissertation develops specific hypotheses on how managerial conformism manifests itself in companies that utilize passing-the-baton style managerial succession processes. Section 3.1 presents the hypotheses on the existence of managerial conformism and agency costs in probationary succession processes, while section 3.2 develops hypotheses on the factors that affect the level of managerial conformism.

3.1. Existence of Managerial Conformism and Agency Costs During Probationary (Relay-Type) Succession Processes

If managerial conformism exists in firms with probationary succession processes, then the performance of these firms would be affected. Performance is measured using operating performance, abnormal stock returns and the number of policy decisions. In short, if the new CEOs conform to the status quo of the firm during their probationary period, the performance of these firms should remain unchanged during the probationary period. Yet, performance is expected to increase significantly once the new CEO passes the test and gets the combined CEO and chairman of the board title.

Managerial conformism is not necessarily detrimental to the firm, however. The reaction from the rivals of the firm would determine whether managerial conformism is necessarily a bad thing. Stock prices of rival firms should react positively if managerial conformism is detrimental to my sample firm, and react negatively if conformism is expected to have good results for the sample firm. The following sections develop these hypotheses in detail.

3.1.1. Operating Performance

Huson, Malatesta and Parrino (2001) provide evidence that measures of abnormal accounting performance in firms decline before managerial turnover events yet improve

subsequently after the turnover. They also find that the managerial turnover announcements are associated with significantly positive abnormal stock returns. These returns are positively related to subsequent changes in accounting performance, suggesting that investors typically view turnover announcements as good news because they anticipate that the turnover will prompt performance improvements.

If agency conflicts between the chairman (retired CEO) and the new CEO lead to managerial conformism, then the new CEO is expected to act along the lines of his predecessor at least until he gets the combined title. In this case, there should be no significant changes in the operating performance of the firm. However, when the probationary period is over and the new CEO has the combined title, he has less pressure (incentives) to conform. Therefore his potential improvements in the firm are expected to surface and operating performance of the firm is expected to improve.

H_1: If managerial conformism exists in passing-the-baton type CEO successions, there should be no significant change in the operating performance of the firm during the probationary period.

H_2: If managerial conformism exists in passing-the-baton type CEO successions, there should be a significant increase in the operating performance of the firm upon the conclusion of the probationary period when the new CEO gets the combined CEO/chairman title.

According to Vancil (1987) passing-the-baton type succession processes also help the board of directors to effectively oust the new CEO at the end of the probationary process if he drops the baton. In this case, decisions to oust the new CEO are expected to

be accompanied by significant decreases in operating performance during the probationary period.

H_3: If, in fact, succession processes are probationary, then declines in operating performance during the probationary period are expected to be followed by the new CEO being ousted.

Brickley, Linck and Coles (1999) argue that accounting and stock performances of the firm affect the post-retirement careers of top-level managers differently. They find that retention on the CEO's own board is primarily dependent on stock returns, while the service on outside boards depends more on accounting measures. Since retiring CEOs would like to pursue either path, or sometimes both paths at the same time, I would expect both accounting and stock based measures of operating performance to exhibit similar effects.

3.1.2. Policy Decisions

Since most of the reputation of a CEO depends on the policies he implements, the former CEO (incumbent chairman) would like to ensure those policies are kept and followed. Additionally, the new CEO would have incentives to conform and keep the status quo to curry favor and pass the transition period as quickly as possible. Thus, there should be significantly more numerous policy changes after the transition period is over and the new CEO obtains both titles.

H_4: If managerial conformism exists in passing-the-baton type CEO successions, there should be no significant change in the number of major policy decisions made by the firm during the probationary period.

H_5: If managerial conformism exists in passing-the-baton type CEO successions, there should be a significant increase in the number of major policy decisions made by the firm upon the conclusion of the probationary period when the new CEO gets the combined CEO/chairman title.

3.1.3. Rival Firms' Reactions

Managerial conformism is not necessarily costly. For an established, stable corporation that has been performing better than their industry average under their current management, making sure the newcomer conforms to the status quo may not be detrimental. Having the departing CEO continue to serve on the board as chairman can reduce information transfer costs and lead to a smooth succession in these firms. Accordingly, Parrino (1997), Huson, Malatesta and Parrino (2001) and Naveen (2003), find that probationary succession processes tend to be concentrated more in heterogeneous industries with large and established firms, while outside succession is more likely to occur in more homogeneous industries with lower human capital needs.

However, for firms that have been underperforming their industry, the costs of managerial conservatism can be higher and succession-securing behavior can be detrimental. In this case, the close competitors of the firm in the same industry should react positively to the company's managerial turnover announcement. Similarly, if managerial succession is not expected to be detrimental to the firm, then the rivals should react negatively to the announcement.

H_6: Announcements of potentially costly managerial conformism are expected to be accompanied by a positive stock price reaction from the firm's competitors, while announcements of potentially beneficial managerial

conformism are expected to be accompanied by a negative price reaction from competitors.

3.2. Factors that Affect the Level of Managerial Conformism

The more incentive conflicts that arise between the incumbent and the new CEO, the harder it would be for the new CEO to successfully complete the probationary period. Thus, the probationary period would take longer. The length of the probationary period will increase with the level of incentive conflicts and agency costs during the probationary period.

H_7: The probationary period should be longer, the higher the level of agency conflicts between the incumbent and the new CEO.

3.2.1. Departing CEO or Chairman Stock Ownership

The conflicts of interest between the former and the new CEOs in a passing-the-baton process, may lead to increased informational asymmetries and agency costs between the CEO and the board of directors. This would bring into question the efficiency of the Board of Directors as a mechanism to monitor top management and to reduce the agency costs between the managers and the shareholders. Thus, in the spirit of Alchian and Demsetz (1972), 'who monitors the monitor?': If the chairman is a large residual claimant, then this problem is solved as in the classical model of the entrepreneurial owner, but in the large complex company, it is generally the case that no one on the board of directors has greater reputational and financial capital at stake in the future performance in the company than does the CEO. As the percentage share ownership of the former CEO or the current chairman declines, agency conflicts between the chairman and the CEO are likely to increase. In this case, the presence of outside

board members and their effectiveness in monitoring the CEO and the chairman become crucial issues in corporate governance.

H_8: Higher stock ownership by the former CEO should align his incentives with those of the shareholders and reduce the probability of managerial conformism.

3.2.2. Managerial Entrenchment

The conflicts of interest between the departing and the incoming CEOs should be worse, the more entrenched the former CEO is to the company. For example, if the former CEO is the founder of the company or a member of the founding family, and he is handing the office of the CEO to an out-of-the family director/manager/president, then he would have greater incentives to try to insure that his successor follows the policies maintained by the founding family for years, which the former CEO, the current chairman himself represents. There are greater benefits to founding families from preserving control in their companies than to professional managers under any circumstance. Burkart, Panunzi and Shelifer (2003) identify these benefits as:

- Amenity potential, using the term coined by Demsetz and Lehn (1985), where there are non-pecuniary private benefits of control, meaning extra utility for the founder that does not come at the expense of profits. Founder may take personal joy at seeing his son run the company that bears the family name.
- Name itself as a carrier of reputation in economic, political and social environments. Such reputational benefits will be diluted if control of the company is surrendered to an outsider.

- Possibility of expropriation of outside investors comes with control (Jensen and Meckling, 1976), and these benefits come at the expense of profits accruing to outside investors. If professional management is employed, then it is now the professional manager, not the founding family that has control of the company and can expropriate outside investors.

Empirically, Andersen and Reeb (2003) find evidence that when founding family members serve as the CEOs of their firms, firm performance is better than when the CEO is an outsider.

H_9: If the departing CEO is a founding family member, the likelihood of managerial conformism should be higher.

H_{10}: If the departing CEO is a family member and the new CEO is a non-family member, then the probability of managerial conformism should be higher than it would be if the incoming CEO is another family member.

Managers get more entrenched to their firms the longer they are employed by the firm or the longer they stay in a certain office. Thus, the longer the former CEO has been in office, the greater would be his attachment to the projects he has started or the policies he has implemented. Simultaneously, a more entrenched departing CEO, whether a member of the founding family or with long tenure, would have closer relationships with board members. Thus, he would have a greater influence on the directors, increasing his chances of influencing the new CEO while decreasing the effectiveness of the board as a monitoring entity. In both cases, the entrenched departing CEO would have a greater felt presence in the corporate culture, which would also increase the incentives of the new CEO to conform.

H_{11}: The longer the departing CEO has been in office, the greater should be the likelihood of managerial conformism.

H_{12}: The longer the departing CEO has been an employee of the firm, the more entrenched he is, and the greater should be the likelihood of managerial conformism.

3.2.3. The Incomer's Stock Ownership and Entrenchment to the Company

In most cases, the incoming CEO is an heir apparent, usually the COO or the president of the firm. The incoming CEO, therefore, has some (and occasionally significantly long) tenure in the firm. In these cases, problems of managerial conformism should be alleviated to a certain degree, since the incoming CEO also has a certain level of attachment and entrenchment to the firm. Especially, if the incoming CEO has significant stock ownership in the firm, then his incentives would be aligned with those of the shareholders. This may reduce managerial conformism to a certain degree.

H_{13}: The longer the incoming CEO has been an employee of the firm, the lower should be the likelihood of managerial conformism.

H_{14}: The higher the stock ownership of the incoming CEO, the lower should be the likelihood of managerial conformism.

3.2.4. Effective Board and Outside Monitoring

The effectiveness of the board of directors in monitoring the top-management will decrease the probability of managerial conformism. Increasing board size decreases the monitoring efficiency of the board of directors on management (Lipton and Lorsch (1992), Jensen (1993)). Both papers argue that as the number of directors on the board of a company increases, boards become less effective monitors. This, in turn increases the

power of the CEO and thus increases the likelihood of managerial conformism. Consistent with these arguments, Yermack (1996) documents a negative relationship between board size and Tobin's Q.

H_{15}: The larger the size of the firm's board of directors, the higher should be the likelihood of managerial conformism.

The proportion of outside directors on the board, on the other hand, increases the monitoring effectiveness of the board, and thus lowers the likelihood of managerial conformism. Consistent with this hypothesis, Ryan and Wiggins (2004) document that firms with more outsiders on their boards award directors more equity based compensation, aligning their incentives better with the shareholders. They argue that this is because outside directors have a greater bargaining power over the CEOs. If directors incentives are more aligned with those of the shareholders, they are likely to be better monitors of the management, decreasing the likelihood for managerial conformism.

H_{16}: The higher the percentage of outside directors in the board of directors, the lower should be the probability of managerial conformism.

Similarly, as institutional stock ownership increases, agency costs decrease. The cost of monitoring management is lower for institutional investors, making them an independent source of monitoring on behalf of the shareholders. Therefore, firms with higher institutional holdings are less likely to experience costly managerial conformism.

H_{17}: The higher the institutional ownership in the firm, the lower should be the probability of managerial conformism.

As stock holdings of board members increase, their interests become more aligned with those of the shareholders, increasing the monitoring efficiency of the board of

directors. Perry (1999) documents that stock based compensation for outside directors increases the likelihood of CEO turnover and improves the monitoring quality of the board in general by aligning the interests of the directors with those of the shareholders.

H_{18}: The higher the stock ownership of non-CEO, non-chairman board members, the lower should be the likelihood of managerial conformism.

3.2.5. Post-retirement Career Opportunities

The retention of a departing CEO on his own board or his employment on the board of another firm depends on the performance of his firm during his tenure as the CEO. Therefore departing CEO will have incentives to encourage managerial conformism during the probationary period in order to secure their future employment.

H_{19}: Retiring chairmen that remain on their own boards after they relinquish the chairmen title are expected to have stronger incentives for managerial conformism.

H_{20}: Retiring chairmen that serve on boards of directors of other firms should have stronger incentives to promote managerial conformism.

On the other hand, an efficient labor market will consider the succession-securing incentives of the former CEO that stays on as the chairman of the board. Therefore, such CEOs would be less likely to end up in comparable board membership positions. Therefore, the post-retirement career of the chairman can provide a measure of his reputation, and might work to reduce the incentives to ensure managerial conformism.

3.2.6. Ease of Comparison and Monitoring

It would be easier and less costly to hire outsiders for top executive positions in markets that are more homogeneous and in industries that are less human capital

intensive. Information transfer costs are lower in these markets, making outside succession a more feasible alternative. Thus, managerial conformism would be less likely in homogeneous industries. Parrino (1997), Huson, Malatesta and Parrino (2001) and Naveen (2003), find that probationary succession processes tend to be concentrated more in heterogeneous industries with large and established firms, while outside succession is more likely to occur in more homogeneous industries with lower human capital needs. Parrino (1997) uses the correlation between common stock returns within two-digit SIC industries as a proxy for industry homogeneity. Additionally, information transfer costs are higher in industries with more firm-specific human capital, which makes outside succession harder in these industries and increases the probability of managerial conformism.

H_{21}: Larger and older firms should be more likely to have probationary planned succession processes.

Firms with more complex organizational structures, such as diversified firms, require a high level of firm-specific human capital. Naveen (2003) and Berry, Bizjak, Lemmon and Naveen (2003) argue that diversified firms are more likely to appoint an insider as CEO and are more likely to engage in succession planning. Similarly, Brickley, Linck and Coles (1999) provide evidence that the post-retirement employment opportunities of executives on other firms' boards are dependent on accounting returns and probability of retention on their own boards is based on stock returns. Since diversified firms are harder to compare to competitors, the evaluation criteria become vaguer, increasing the stakes and the agency conflicts. Furthermore, since diversified

firms are harder to monitor, they are more prone to agency conflicts and succession securing behavior.

H_{22}: Diversified firms are harder to monitor, so they should have higher succession-related agency costs.

Information asymmetries between the managers and the market are greater in firms with high growth potentials, which makes them harder to monitor. Therefore, firms with high growth opportunities are expected to have higher probabilities of managerial conformism.

H_{23}: Firms with higher market-to-book ratios would be harder to monitor so should have a higher probability of managerial conformism.

CHAPTER 4
SAMPLE SELECTION AND METHODOLOGY

4.1. Sample Selection and Data Collection

4.1.1. Management Data

The initial sample for this dissertation includes all the firms that have announced a change to their top management positions, namely CEOs and chairmen of the board, during the period from 1993 to 1995. I gather the firms to be included in the sample using a keyword search on Lexis-Nexis of the major news and wiring resources for news announcements and articles containing the words, 'CEO', 'chief executive' or 'chairman' and verbs such as 'choose', 'appoint', 'name', 'select', 'retire', 'resign', 'elect' or 'leave' for the years 1993 through 1995[7]. I then classify the firms as dual leadership firms, firms that change either their CEO or chairman or both, unitary leadership firms that change their chairman/CEO, or firms that change from unitary to dual leadership or vice versa. Of the firms that change from unitary to dual leadership or vice versa, I separate those that are following a planned relay-type succession plan as the passing-the-baton sample. I identify the firms with probationary succession processes from the explanation in the news article or by following the company through the years in both Lexis Nexis and in proxy statements. If the managerial turnover announcement specifically states that the departing CEO remains on the board as the chairman, I follow it through on Lexis-Nexis to determine the time boundaries on the probationary period. This yields a sample of 2,154 announcements by 1,923 firms. After excluding the announcements made by

[7] Brickley, Coles and Jarrell (1997) are the first to use such a methodology. They search for *Wall Street Journal* announcements containing the words 'chief executive officer' and 'chairman' and the verbs 'choose, appoint, name or select'. The methodology utilized in this paper improves upon their methodology. This proves to be a more comprehensive sample than just using the 800-1000 firms in the Forbes Executive Surveys like most of the previous literature.

foreign or private firms and subsidiaries that do not trade separately, I have a sample of 1,339 announcements by 1,295 firms.

I verify the events and their dates by their appearance in the *Wall Street Journal*, and assume the event day to be the first day any news of the managerial change appears in the *Wall Street Journal* or any other major news wire or source. From the remaining 1,339 announcements, I remove the 44 announcements made about CEO or chairman changes around reorganizations, bankruptcies or going private transactions where public information is not available. Of the remaining 1,293 managerial changes, 527 (40.76 %) are passing-the-baton type probationary succession processes; 458 are announcements made by firms that have a dual leadership structure and are changing either their chairmen or CEOs or both; and 208 (16.08 %) announcements are from firms that have unitary leadership, and the same individual that holds the CEO and chairman title changes. In the 458 announcements from dual leadership firms, 287 (62.66 %) announce a change of only the CEOs while the chairmen stay the same; 119 (25.98%) announce a change in the chairmen while the CEOs stay the same; and the remaining 52 (11.35 %) announce a change of both their CEOs and chairmen at the same time. The remaining 100 announcements in the sample are separated as 73 announcements of firms with unitary leadership separating their titles (not for a probationary period but rather permanently) and 27 announcements from firms with dual leadership that combine the CEO and chairmen titles.

I then follow the succession process of every firm through using news articles about the firm in Lexis-Nexis and the *Wall Street Journal Corporate Index*, as well as the

managerial and board membership changes stated in proxy statements. For the passing-the-baton sample, I identify two dates:

- date when the former CEO and chairman of the board relinquishes the CEO position to his heir apparent to remain as the chairman of the board (beginning date for the probationary period)
- date when the chairman (former CEO) finally retires from executive duties by retiring as the chairman as well and the new CEO is granted the combined CEO and chairman of the board title (ending date of the probationary period)

Interim office holders are not included in the sample. However, if the interim CEO or chairman becomes the permanent office holder, then the period of time they have been in office (or in other words, the time they are appointed) is adjusted to include the period where they serve as an interim officer. For example, when J.P. Bolduc, the chief executive of W.R. Grace & Co resigned from his duties on March 2, 1995, the board appointed Thomas Holmes, a senior vice president of the firm at the time, to succeed Bolduc for a temporary period. Thomas Holmes was appointed as the permanent CEO of W.R. Grace & Co on November 12, 1995. In this case, I use the initial date of appointment, March 2, 1995 as the date Holmes becomes the CEO of W.R. Grace & Co. Similarly, if the interim CEO is part of a passing-the-baton process, and he becomes the permanent CEO, the length of his probationary period has been adjusted to include the time when he served as an interim or acting chief executive. On the other hand, if the interim office holder is replaced eventually for a permanent placement, I exclude the interim office holder from the sample, and treat these two announcements as one single

succession process. This process reduces the sample size from 1,293 announcements to 1,057 announcements made by 978 firms.

I note the reason for every CEO or chairman departure. Following Naveen (2003), I classify all CEO departures that are reported in the financial press as forced departures as such. Additionally, I consider any departure of a CEO under the age of 60 leaving for reasons other than death, health, family matters or acceptance of any position within or outside the firm are considered as forced departures.

I obtain the information on the ages and tenures of the CEOs and chairmen at the time they are appointed and when they retire as well as the total time they have worked for the company from the news announcements and double-check them with the information from proxy statements. Table 1 presents a summary of all the data used in this dissertation and their sources.

Additionally, I collect information on the origins of the new CEOs and chairmen from the news announcements and proxy statements. For companies that choose to promote from within, I note the last office the new CEO has held. If the new CEO is an outsider, then I identify the company the new CEO comes from. In addition to the names of the companies, I create a dummy variable that takes the value of one if the new CEO or chairman is an outsider. In my sample, the new CEOs recruited from other companies tend to be either from companies in the same industry or partners of management consulting, accounting/auditing or law firms of which he company is a major client. I create different dummy variables for each of these cases.

Table 4.1
List of Variables and Their Sources

This table presents the main groups of data used in this dissertation and the various sources it is obtained from. The details of the searches and the exact variables collected from these sources are detailed in the text. This table provides a summary.

Data	Source
Exact dates of succession details	Lexis-Nexis news announcements
Details of the succession process	Lexis-Nexis news announcements and proxy statements
Reason for managerial departure	Lexis-Nexis news announcements
Manager's age	Lexis-Nexis news announcements and proxy statements
Manager's tenure	Lexis-Nexis news announcements and proxy statements
Manager's time spent with the company	Lexis-Nexis news announcements and proxy statements
Origin of the new manager	Lexis-Nexis news announcements and proxy statements
Post-retirement careers of departing managers	Lexis-Nexis news announcements and proxy statements
Firm's board size	Proxy statements
Percentage of outside directors on board	Proxy statements
Percentage share ownership of executives	Proxy statements
Accounting data	Research Insight
Stock return data	CRSP
Industry specification (SIC codes)	Research Insight
Number of business segments of the firm	Research Insight
Institutional Ownership	Compact disclosure
Number of policy decisions	Lexis-Nexis news announcements

Furthermore, I follow the post-retirement careers of the departing CEOs and chairmen in order to determine whether post-retirement careers provide incentives for them to encourage managerial conformism. Most of this information is available through Lexis-Nexis searches of news announcements for the name of the chairmen and have been verified from proxy statements, when necessary. Consistent with Brickley, Linck and Coles (1999) and Sonnenfeld (1988), retiring chairmen follow one of three paths: continue to serve on the boards of their own companies as chairmen emeriti, non-

executive directors, chairmen of the executive committee or consultants and advisors; serve on the boards of other companies that they are either already part of before they retire or they become part of as they retire; or just retire or form their own small entrepreneurial business. Reputational incentives are very low, if not nonexistent in the last scheme. However, in the first two cases where the retiring chairmen continue to work as members of their own or other firms' boards, reputational incentives underlying succession-securing behavior are influential. I create dummy variables taking the values of one if the chairman continues on his own board and if he serves on other boards.

Some firms with dual leadership that prefer to groom managers from within have an intermittent step between the titles of CEO and chairman of the board. In these firms departing CEOs become vice-chairmen and stay on the board. When the current chairman retires, the vice-chairman becomes the new chairman. This is another form of relay-type processes where the CEO and chairman titles do not overlap. I create another dummy variable denoting this type of succession process in order to distinguish these firms from other firms with dual leadership.

4.1.2. Firm and Performance Data

Brickley, Linck and Coles (1999) find that retention on the CEO's own board after retirement depends primarily on stock returns, while service on outside boards is better explained by accounting returns. Thus, I collect stock return data and accounting data used to measure the operating performance of the firm from the Center for Research on Security Prices (CRSP) and Research Insight (COMPUSTAT) databases respectively.

Similarly, data for other firm specific variables, like firm age, the two-digit and four-digit primary SIC codes for the companies and the number of business segments, are

also from the Research Insight (COMPUSTAT) database. Institutional ownership information is collected from Compact Disclosure.

I determine the numbers of policy changes during the transition period as well as the ones after the new CEO gets the combined title again using a keyword search on Lexis-Nexis news and wire sources for the news articles containing the name of each company. I remove earnings announcements, financial report filings and reviews of the company by other institutions, including financial institutions, analyst forecasts and rating agencies. I consider all other events as policy decisions, and use the number of policy changes during the transition (probationary) period and before the start of and after the completion of the transition period as separate variables.

I gather other firm specific variables like board size, stock ownership of the chairman, the CEO and the board members as well as the existence and the percentage of outside directors from proxy statements of the firm published at the end of the fiscal year prior to the announcement. Board members that are (or have been) executive officers or direct employees of the firm, employees of direct customers or suppliers of the firm or members of the founding families that may have seats on the board are considered inside directors. Additionally, I also consider employees of commercial or investment banks, venture capital firms, insurance companies, audit companies or law firms that may have direct business relationships with the firm as inside directors. I classify the remaining independent board members as outside members.

As mentioned in the previous section, managerial conformism is not always and necessarily detrimental to the performance of a firm. For older, more stable firms with higher firm-specific human capital, managerial conformism can potentially be an

efficient means of information transfer between the top management of the firm. The reaction of a firm's rivals to the announcement of managerial turnover and relay-race type succession process should be related to whether managerial succession is costly to the company or potentially beneficial. I determine the rivals of sample firms based on two-digit and four-digit SIC codes. The accounting and stock price information for the rivals also come from the Research Insight (COMPUSTAT) and CRSP databases.

Availability of proxy statements for all the necessary years as well as the availability of data on CRSP, Research Insight and Compact Disclosure simultaneously reduces the sample size in this dissertation to 475 announcements made by 473 companies.

4.2. Methodology

This dissertation uses data from announcements made during 1993 through 1995 in order to allow for a time period of at least three years after the new CEO has been granted both titles and sufficient time has passed for him to implement his policies and for changes in operating performance to occur. For instance, Graco Inc announced on December 15, 1995 that its chairman and chief executive officer, David Koch has resigned from his executive duties, but he will remain as the chairman of the board of directors. Koch and his successor as CEO, George Aristides, served together for a probationary period of approximately 2.5 years and Aristides was granted the combined CEO and chairman of the board title on June 23, 1998. I allow for a period of at least three years after the new CEO obtains the combined title for comparison purposes, which brings data up to June 2001. Therefore, for announcements made later than 1995, I may

run into data unavailability problems in cases of long probationary periods. Thus, the time period for the announcements ends at the end of the year 1995.

I use three years as the basis period for operating performance comparisons between different managers and different periods, since Gabarro (1987) finds three years to be the typical time period over which new executives introduce major changes to their organization[8].

I divide the sample into three major groups: relay-race type (probationary) managerial succession processes; managerial turnover in firms with dual leadership (either the CEO or the chairman changes or both change simultaneously); managerial turnover in unitary leadership firms where the manager holding the combined CEO and chairman title changes. There are 203 (42.74 % of the sample) announcements of probationary or in other words passing-the-baton type, managerial successions. The second category with dual leadership firms changing either their CEO, chairman or both simultaneously includes 90 announcements. Of this 90 (18.95 % of the sample), 48 firms (53.33 %) change only their CEOs and 34 (37.78 %) change only their chairmen while only 8 firms (8.89 %) change both their CEOs and chairmen at the same time. On the other hand, there are 128 firms where the single individual holding the combined CEO/chairman title is replaced by another individual holding the same combined title. Each one of these different methods of succession is analyzed in detail in the following chapter of the dissertation.

The succession process in probationary type successions has three parts:

[8] Khurana nad Nohria (2001) also follow this methodology and use three year periods.

- The before period: three years prior to the announcement that departing CEO and chairman will relinquish his CEO title but will remain on the board as chairman.
- The probationary period (transition period): the period where the old CEO/chairman remains as the chairman and his successor serves the firm as the CEO. This is a temporary period of dual leadership in these firms that are generally run by a single unitary leader with a combined title.
- The after period: three-year post-unification period, after the probationary period is completed successfully and the new CEO is granted the combined CEO and chairman of the board title.

For dual-to-dual leadership and unitary-to-unitary leadership transitions, there are only two periods: a pre-turnover and a post-turnover period. Again, I use a three-year window of operating performance to compare and contrast the performances under both managers.

This dissertation explores two empirical questions: Does managerial conformism exist in probationary succession processes, and what factors affect the level and magnitude of managerial conformism? First, I document the existence of managerial conformism using univariate tests of differences in mean and median measures of operating performance between the three periods of the probationary succession process. I use the number of policy decisions, changes in abnormal returns and changes in accounting operating performance between the transition period and the periods before succession starts and after the new CEO obtains the combined CEO/chairman title to conduct these tests.

Accounting operating performance measures are return on assets (ROA) and industry adjusted returns on assets (IAROA), following Baliga et al (1996) and Brickley, Linck and Coles (1999).[9] Return on assets is the average return on assets over these periods, calculated as the net income divided by average assets. Following Parrino (1997) and Naveen (2003), industry-adjusted return on assets have been defined as the average annual returns on assets net of the industry mean, where the industry is determined according to two-digit SIC codes.[10] I also use the Barber and Lyon (1997) criteria to create matched samples of firms, and report both results in Chapter 6.

Mean abnormal stock returns are the returns on the security reported by CRSP net of the returns on the CRSP value-weighted index, following Baliga et al (1996) and Brickley, Coles and Jarrell (1997), and industry adjusted mean abnormal returns are the mean abnormal returns net of the industry average mean abnormal returns for the corresponding period, using two-digit SIC codes to determine industry (Parrino, 1997).[11] Similar to accounting performance, I re-do the same analysis using Barber and Lyon (1997) matching criteria for robustness.

The factors that determine the level of managerial conformism are determined as a result of multivariate regression analyses presented in Chapter 7. I use the length of the probationary period as a dependent variable in regular OLS regressions.

[9] Other measures of operating performance, like return on capital following Brickley, Coles and Jarrell (1997), return on equity (ROE) and return on investment (ROI) have been considered. However, tests have revealed similar results with all three proxies, therefore only ROAs are reported.

[10] The industry-adjusted operating performance and market reaction variables are also calculated using four-digit SIC codes and the results are similar. Therefore, to be consistent with previous literature, two-digit SIC code based results are reported.

[11] The results for mean abnormal returns are checked for robustness by substituting the CRSP equally-weighted index instead of the value-weighted index. The empirical results remain unchanged under different market proxies, therefore, consistent with previous literature, only the results using the value-weighted index are reported.

The dependent variable used in the logit regressions measuring the probability of managerial conformism equals one if the incumbent CEO of the company shows managerial conformism. This variable is set to equal one if there is an increase in the number of policy changes after the transition period is over, there is a significant increase in the operating performance of the firm measured both by industry adjusted return on assets and industry adjusted returns.

Sixteen different independent variables are considered to as proxies for the factors that affect the level of managerial conformism in firms. However, due to the multi-collinearity between these independent variables in the regressions, a principle components analysis has been conducted to yield five major components to be used in the rest of the analysis in Chapter 7. The five components with eigenvalues greater than one have been included in the regressions that measure the level of managerial conformism in firms.

CHAPTER 5
SAMPLE CHARACTERISTICS AND DETAILS OF MANAGERIAL SUCCESSION PROCESS IN THE U.S.

Three main channels of CEO succession dominate the contemporary corporate world. Firms that have a single individual holding the combined CEO and chairman of the board title either choose to follow a relay-race type (probationary) succession process or choose to replace their CEO and chairman with a new individual holding both titles. In a probationary succession process, the incumbent CEO and chairman of the board initially relinquishes only his CEO title to the heir apparent while maintaining his chairman of the board title. The new CEO and the departing CEO, currently chairman, then manage the company together for a probationary period. Upon successful completion of this period, the new CEO also obtains the chairman of the board title and the previous CEO retires from both of his duties. On the other hand, a company with unitary leadership may choose to replace the individual holding the combined CEO and chairman of the board title with a new individual that will also immediately hold a combined CEO/chairman of the board title. I have named this latter managerial turnover event as a unitary- to-unitary succession.

Firms that have dual leadership structures, meanwhile, change either their CEOs only, their chairmen only or both simultaneously. I refer to this group as dual-to-dual successions. The remaining succession announcements include firms that have unitary leadership structures, but announce that the separation of their CEO and chairman of the board titles. Similarly, some announcements are by firms that have separate chairmen and CEOs and decide to combine the titles. I grouped these firms under separation of

titles and unification of titles groups. The details of these different succession processes are presented below.

Table 5.1
Descriptive Statistics: Entire Sample

Panel A presents the descriptive statistics of the entire sample. CEO and chairmen ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. Probationary period is the number of years it takes for new CEO to be granted the combined CEO/Chairman of the Board title, during which the old and the new CEO work together. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Market capitalization of the firms are also presented in millions of dollars. Panel B displays the percentage of firms in the sample that prefer different succession types as well as the exchanges they trade on.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing Chairman Age	475	60.21	8.55	35	54	62	66	85
Departing Chairman Tenure as Chairman	475	8.26	7.67	0.08	3	6	11	47
Departing Chairman Prior Time with the Firm	475	18.77	13.20	0.08	7	15	30	52
Departing Chairman Share ownership (%)	475	5.72	0.11	0	<1	1.30	6.10	68.20
Departing CEO Age	475	58.32	8.63	35	52	60	65	78
Departing CEO Tenure as CEO	475	8.18	7.52	0.08	3	6	11	47
Departing CEO Prior Time with the Firm	475	17.68	13.07	0.08	7	13	28	52
Departing CEO Share Ownership (%)	475	4.56	9.22	0	<1	1.11	4.18	68.20
Incoming Chairman Age	475	53.31	8.68	31	47	53	59	76
Incoming Chairman Prior Time with the Firm	475	10.07	11.20	0	1	7	16	47
Incoming Chairman Prior Time as a director on the board	475	6.14	8.32	0	0.20	3	8	47
Incoming Chairman Share ownership (%)	475	3.92	9.96	0	<1	<1	2.77	91.01
Incoming CEO Age	475	50.87	7.28	31	46	51	56	77
Incoming CEO Prior Time with the Firm	475	8.35	10.27	0	0	4	13	47
Incoming CEO Prior Time as a director on the board	475	3.81	5.04	0	0	2	6	31
Incoming CEO Share Ownership (%)	475	2.31	7.27	0	<1	<1	1.7	91.01
Board Size	475	8.90	3.32	3	6	8	11	24
Outside Board Members (%)	475	36.99	16.06	0	25	37.5	50	85.72
Institutional Ownership (%)	475	31.78	14.67	0.31	11.93	37.92	55.45	91.03
Board Stock Ownership (%)	475	6.94	11.23	<1	0.44	3	8.20	88.23
Market Capitalization ($ millions)	475	1512.75	5725	0.35	18.36	100.54	752.50	77591

(table continued)

Panel B: Succession Details

	Number	% of Sample
Passing-the-baton (probationary) succession	203	42.74%
Unitary-to-unitary leadership succession	128	26.95%
Dual-to-dual leadership	90	18.95%
CEO change only	48	10.11%
Chairman change only	34	7.18%
Both CEO and chairman change simultaneously	8	1.68%
Separation of leadership	39	8.21%
Unification of leadership	15	3.16%
Firm is listed on NYSE	226	47.58%
Firm is listed on NASDAQ	208	43.79%
Firm is listed on AMEX	26	5.47%

Table 5.1 presents the distribution of the sample across different succession methods as well as the descriptive statistics of the entire sample. Out of the 475 different succession events included in my sample, 203 (42.74% of the entire sample) are probationary succession processes, while in 128 (26.95%) of the succession events, the individual holding the combined CEO and chairman of the board title is replaced in both functions by a new individual holding the same combined title. This shows that 70% of the firms still prefer to have unitary leadership structures. Out of the 90 firms (18.95%) in my sample that have dual leadership structures, more than half, 48 (10.11% of the entire sample), choose to change only their CEOs while their chairmen stay the same, while 34 firms (7.18% of the entire sample) change only their chairmen of the board while their CEOs stay the same. Only eight firms out of my entire sample of 475 (1.68%) choose to change both their CEO and chairman at the same time. Of the remaining 54 firms, 39 (8.21% of the entire sample) separate their CEO and chairman of the board titles and move from a unitary to a dual leadership structure, whereas 15 (3.16% of the entire sample) move the opposite way and combine their CEO and chairman of the board titles under one individual.

My sample is well distributed among firm sizes and exchanges as well. The average (median) firm in my sample has a market capitalization of $1,512.75 ($100.54) millions. Firm sizes range from $0.35 million in market capitalization to $77,591 million. Out of the 475 firms, 226 firms (47.58%) trade on the NYSE, 208 (43.79%) trade on NASDAQ and 26 firms (5.47%) trade on the AMEX.

The average (median) age for departing chairmen in the overall sample is 60.21 (62), and they served on average (median) 8.26 (6) years as chairmen and on average (median) 18.77 (15) years in various positions in their companies. The departing CEOs are approximately two years younger, where the average (median) age of a departing CEO is 58.32 (60). Most departing CEOs have on average (median) 8.18 (6) years tenure as CEOs and on average (median) 17.68 (13) years of service in the company. The average (median) stock ownership for departing chairmen and CEOs is 5.72% (1.30%) and 4.56% (1.11%) respectively.

The incoming chairmen are on average 6.82 years younger than the departing ones (this difference is significant with a t-statistic of 14.24). The average (median) age of incoming chairmen of the board is 53.31 (53) and they have worked an average (median) of 10.07 (7) years in the firm, and have served an average (median) of 6.14 (3) years on the board of directors of these institutions. Similarly, the incoming CEOs are on average 7.58 years younger than their predecessors (significant difference with a t-stat of 16.17) with an average (median) 50.87 (51) years old. They have an average (median) tenure of 8.35 (4) years in the firm and an average (median) tenure of 3.81 (2) years as directors on the board. The incoming chairmen and CEOs have even lower shareholdings compared to their departing counterparts. The percentage share ownership in the firm of

incoming chairmen and CEOs are on average (median) 3.92% (less than 1%) and 3.81% (2%), respectively.

The firms in my sample have average (median) board sizes of 8.90 (8) members and on average (median) 36.99% (37.5%) of the directors on board are outsiders[12]. The members of the board, except for the chairman and the CEO, own on average (median) 6.94% (3%) of the outstanding stock in the firms in my sample. Institutional investors, on the other hand, own on average (median) 31.78% (37.92%) of the shares in the firms in my sample.

Firms included in may sample are evenly distributed through industries (See Table 5.2). No single industry is dominant. Chemical and allied products industry has the highest concentration of firms with 43 firms, less than 10 % of the sample belonging in that category.[13]

5.1. Relay-race Type (Probationary) Managerial Succession

In my sample, 203 out of the 475 managerial succession announcements are of probationary (passing-the-baton type) succession processes. Table 5.3 presents the descriptive statistics for this sub-sample. The departing CEOs in my sample are on average (median) 60 (63) years old and have been employed an average (median) of 20 (17.5) years by their companies. The mean (median) tenure of the departing CEO and Chairman as chairman on the board is 8.6 (7) years while his mean (median) tenure as the CEO is 9.7 (8) years.

[12] Outside directors are defined as those directors who are not (have never been) employees of the company, and have no direct business relationship with the firm as a customer, supplier, shareholder, consultant, auditor, banker, investment banker, venture capitalist, attorney…etc.

[13] Similar industry classifications have been documented for each type of managerial succession. No specific industry dominates any one of the succession methods, therefore they are not presented.

Table 5.2
Industry Classifications for the Firms in the Sample

This table presents the industry classification of the firms in the sample. SIC codes are available for 399 firms out of the 475 included in the sample, and the distribution of the firms across industries is provided based on their 2-digit SIC codes.

Industry	2-digit SIC Code	Number	% of Sample
Mining	10	5	1.05%
Oil and Gas	13	9	2.95%
Construction	15-17	3	0.63%
Food Manufacturing	20	8	1.68%
Tobacco	21	1	0.21%
Textile and Apparel Manufacturing	22-23	8	1.68%
Wood, paper and allied products	24-26	11	2.32%
Printing and Publishing	27	6	1.26%
Chemical and allied products	28	43	9.05%
Petroleum, coal, rubber and leather	29-31	11	2.32%
Stone and glass	32	4	0.84%
Metal industries	33-34	6	1.26%
Industrial Machinery and equipment	35	34	7.16%
Electronics and other electronic equipment	36	33	6.95%
Transportation	37	6	1.26%
Instruments	38	22	4.63%
Other manufacturing	39	7	1.47%
Transportation	40-47	14	4.42
Communication	48	4	0.84%
Public utilities	49	19	4.00%
Wholesale trade	50-52	15	3.16%
Retail trade	53-59	34	7.16%
Finance, Insurance and Real Estate	60-66	26	5.47%
Holding companies	67	26	5.47%
Personal Services	72	4	0.84%
Business Services	73	23	4.84%
Motion pictures and amusement and recreation services	78-79	5	1.05%
Health services	80	6	1.26%
Other services	81-89	6	1.26%

Upon departure, the old CEOs and chairmen have on average (median) 4.9 % (1.35%) share ownership in the company. More than 75 % of the departing chairmen in the probationary succession sample have less than 5% ownership in the company, and more than half have less than 1.5 %, making stock ownership an inadequate means to align the incentives of the departing chairmen with those of the shareholders. Similarly, 118 (58.13%) of the departing chairmen are 60 or older, in other words, close to retirement

age, consistent with Vancil's (1987) description of the relay-race style succession process as mainly a planned smooth succession process.

Table 5.3
Probationary Succession Processes

Panel A presents the descriptive statistics of the passing the baton sample. CEO ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. Probationary period is the number of years it takes for new CEO to be granted the combined CEO/Chairman of the Board title, during which the old and the new CEO work together. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents the percentage of firms in the sample with incomplete probationary succession processes where the new CEO was ousted before he was granted the combined title or where the heir apparent left the firm before becoming the CEO as well as the exchanges the firms are listed on. Panels C and D present the origins of incoming CEOs and the future career choices of departing chairmen/CEOs, respectively.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing CEO and Chairman Age	203	60.46	8.27	35	56	63	65	78
Departing CEO and Chairman Tenure as Chairman	203	8.63	7.98	0.25	3	7	11	47
Departing CEO and Chairman Tenure as CEO	203	9.68	8.07	0.5	4	8	12	47
Departing CEO and Chairman Prior Time with the Firm	203	20.35	13.50	0.5	9	17.5	31.75	52
Departing CEO and Chairman Share Ownership (%)	203	4.91	9.81	<1	<1	1.35	4.23	62.1
Incoming CEO Age	203	50.09	6.96	34	45	50	55	67
Incoming CEO Prior Time with the Firm	203	9.34	10.93	0	0.29	4	15.5	40
Incoming CEO Prior Time as a director on the board	203	3.68	4.67	0	0	2	5	27
Incoming CEO Share Ownership (%)	203	1.43	3.67	0	<1	<1	1.4	26
Length of the Probationary Period	203	2.46	2.60	0.01	0.75	1.57	3.53	16.34
Board Size	203	9.29	3.26	3	7	9	11	23
Outside Board Members (%)	203	36.91	15.47	0	27.27	37.5	46.96	76.92
Institutional Ownership (%)	203	32.86	12.5395	0.31	12.73	36.79	52.12	87.24
Board Stock Ownership (%)	203	6.72	11.40	<1	<1	2.91	7.49	74.8
Market Capitalization ($millions)	203	1586.14	5126	1.67	16.10	127.53	976.54	44183

(table continued)

Panel B: Succession Details

	Number	% of Sample
New CEOs ousted after transition period	20	9.85 %
Transition period ends with the death of the departing chairman	6	2.96 %
Departing chairmen that are founders or members of the founding family	41	20.20 %
Firm is listed on NYSE	106	52.22 %
Firm is listed on NASDAQ	88	43.35 %
Firm is listed on AMEX	5	2.46 %

Panel C: Incoming CEO Origin

	Number	% of Sample
Incoming CEO is an outsider	55	27.09 %
Incoming CEO was President or Chief Operating Officer	111	54.68 %
Incoming CEO was President or CEO of a subsidiary	10	4.93 %
Incoming CEO was Executive/Senior VP or CFO	15	7.39 %
Incoming CEO was outside director or consultant to the firm	8	3.94 %

Panel D: Departing CEO and Chairman's Future Career

	Number	% of Sample
Departing chairmen that serve on other boards after retirement	87	42.86 %
Departing chairman stays on the board as Chairman Emeritus	18	8.87 %
Departing chairman stays on the board as a director	70	34.48 %
Departing chairman stays on the board as chairman of the executive committee	11	5.42 %
Departing chairman stays on the board as a consultant to the firm	4	1.97 %

The average (median) age of the incoming CEOs is 50 (50), and with an average (median) of 9.43 (4) years spent previously with the company. These incoming CEOs have previously served on the board of directors of the company on average (median) 3.68 (2) years. Though the average new CEO has 1.4 % share ownership in the company when he first assumes the CEO title, the median stock ownership of new CEOs is less than 1%.

Of the 203 firms that prefer probationary succession processes, 55 (27.09%) choose their new CEOs from managers of other firms while eight (3.94%) name either

their chief consultant or one of the outside directors to be the new CEO and subsequently CEO and chairman of the board of directors. There are three main paths to inside succession, however. Out of the remaining 140 firms that promote managers from within the firm to the CEO position, 111 (54.68 % of the entire passing-the-baton sample, and 79.29% of the firms that prefer inside successors) promote their presidents and/or chief operating officers to the CEO office. Ten (4.93 % of the sample) new CEOs are previous heads, presidents or CEOs of the main subsidiaries of the firm, while 15 (7.39 %) are promoted from executive or senior vice presidents or CFOs. This pattern also fits Vancil's (1987) description of probationary succession processes where the departing CEO and chairman chooses an heir apparent, usually the President or COO of the firm, and relinquishes his CEO title to him.

Most of the departing chairmen in my relay-race succession sample continue their professional careers after relinquishing managerial titles. Almost half of the departing chairmen, 87 (42.86 %) to be exact, continue to serve as directors on the boards of other companies after retirement. On the other hand, 18 (8.87 %) departing chairmen remain on the board of directors of their companies as chairmen emeriti, 70 (34.48%) remain to serve as directors on their own boards and 11 (5.42%) continue to be chairmen of the executive committee. Similarly, 4 (1.97%) departing chairmen continue to serve their companies as consultants. Of these departing CEOs, 41 (20.20%) are also founders of their firms or members of the founding family. Since most departing chairmen continue their careers on either their own board or on the boards of directors of other corporations, incentives for managerial conformism exist in the sample.

The average (median) market capitalization of the firms that prefer relay-race type probationary succession processes is $1,586.14 million ($127.53 million). The mean market capitalization is significantly greater than the median because of some large cap companies included in the sample. Some of the largest firms in this sub-sample are Phillip-Morris with a market capitalization of $44,183 million and General Motors with a market capitalization of $21,202 million. The sample includes 106 firms listed on the New York Stock Exchange (NYSE), 88 firms listed on NASDAQ and five firms listed on the American Stock Exchange (AMEX). The average (median) number of directors that serve on the board of directors of firms choosing probationary succession processes is 9.29 (9). On average (median) 36.91 % (37.5%) of the directors are outsiders. Members of the board except for the departing and incoming CEO own on average (median) 6.72 % (2.91%) of the shares of the company. Similarly, institutional ownership in the companies that utilize relay-race type succession processes is 32.86 % (36.79 %) on average (median).

The average (median) length of the probationary period when the old and new CEOs serve together as chairman of the board and CEO, respectively, is 2.46 (1.57) years. The maximum probationary period lasts over 16 years in Collagen Corp, where the departing CEO still continues to remain as chairman emeritus even after relinquishing both titles. On the other hand, the shortest probationary period is less than a week in Indresco Inc where the departing CEO unexpectedly retired at the beginning of the probationary period, after announcing that he would remain as the chairman of the board for another two years, and relinquished his chairman title immediately after the CEO title.

According to Vancil (1987), one of the purposes of the probationary period is to enable the board to effectively oust any new CEOs that "drop-the-baton" or cannot perform satisfactorily. In my sample, 20 firms (9.85 %) end up ousting their incoming CEOs, without passing them the baton. Six succession processes (2.96%), on the other hand, are concluded with the death of the incumbent CEO/current chairman.

5.2. Succession from Unitary Leadership to Unitary Leadership[14]

The term, "unitary leadership firms", in this dissertation, refers to those firms that have a single individual holding the combined CEO and chairman of the board title. There are 128 firms in my sample that have unitary leadership and decide to undergo a managerial change where the individual that holds the combined CEO/chairman title is replaced by another individual that holds the same combined title. Table 5.4 presents the descriptive statistics and the succession details of these firms.

The average retirement age for the departing CEO and chairmen in unitary leadership firms seems a little higher than firms using probationary succession processes. The incumbent chairman and CEO departs on average (median) at the age of 59.41 (62), after serving an average (median) of 7.13 (6) years as the CEO and chairman of the board. On average (median) the departing CEO and chairmen have been employed by their companies 18.99 (16) years, and own on average 4.60 % of the firm's stock upon retirement. The median stock ownership by the departing CEO and chairmen is less than one percent, however. The high averages are the result of 25 (19.53% of the sample) firms where the departing CEO and chairmen are founders or members of the founding family and therefore own sometimes even more than 50% of the stock of the company.

[14] Due to data availability problems, the number of observations for each variable differs in all the subsamples except for the probationary succession sample.

For instance, Morris Dabah, son of Gitano Corp's founder, owns 68.20% of the firm's stock when he retired from his position as chairman of the board and CEO.

The incoming CEO and chairmen of the board are on average (median) 52.93 (53) years old and have been employed by their companies on average 7.95 (3) years, having spent on average (median) 3.39 (1) of these years serving on the board of directors of their companies. Incoming CEOs own on average (median) 4.33 % (less than 1%) of the stock of the company when they are first appointed as the new CEO and chairman of the board. The difference between the mean and median is driven by two extreme cases, Marquest Medical Products, Inc and YES Clothing co, where the controlling shareholders, with 71.99 % and 91.01 % ownership respectively, become the new CEO and chairmen of the board.

Only nine (7.03 %) out of the 128 unitary leadership successions are the result of forced departures of the incumbent CEO and chairman of the board. On the other hand, eight (6.25 %) of the new CEOs have served as an interim CEO and chairman of the board before obtaining the permanent title. Half of the firms in the sample are listed on NYSE, while 54 firms (42.19%) are listed on NASDAQ and 7 (5.47%) are listed on AMEX at the time of the managerial succession. The average (median) size of these firms measured by their market capitalizations is $2,432.21 million ($134.60 million). The firm with the largest market capitalization is Exxon Corp with $77,591.44 million, creating the gap between the mean and the median market capitalization. These firms have on average (median) 9.24 (8) directors on serving on their boards, and on average (median) 43.84% (42.86%) of these directors are outsiders. The directors of the firm except for the CEO and chairman, own on average (median) 7.31% (1.80%) of the shares

in these firms. Similarly, institutional investors own on average (median) 29.92% (29.05%) of the shares in unitary leadership firms that change their leader holding a combined CEO/chairman of the board title.

Table 5.4
Unitary to Unitary Succession

Panel A presents the descriptive statistics of the sample of firms with unitary leadership structures who change their CEO and Chairman of the Board. CEO ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and Chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and chairman and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents certain firm characteristics like the exchanges the firms are listed on, the number of new CEO/Chairman that served as interim office holders before being granted the permanent title, the number of founders and members of the founding family that are relinquishing their titles. Panels C and D present the origins of incoming CEOs and the future career choices of departing chairmen/CEOs, respectively.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing CEO and Chairman Age	108	59.41	7.43	35	53	62	65	72
Departing CEO and Chairman Tenure as CEO/Chairman	102	7.13	5.96	0.08	3	6	10.75	33
Departing CEO and Chairman Prior Time with the Firm	103	18.99	13.08	0.08	8.5	16	28.5	48
Departing CEO and Chairman Share Ownership (%)	112	4.60	10.57	0	<1	<1	3.43	68.20
Incoming CEO and Chairman Age	125	52.93	7.95	31	48	53	58	74
Incoming CEO and Chairman Prior Time with the Firm	121	7.95	10.29	0	0	3	13	38
Incoming CEO and Chairman Prior Time as a director on the board	120	3.39	4.84	0	0	1	4.25	22
Incoming CEO and Chairman Share Ownership (%)	126	4.33	12.39	0	<1	<1	1.92	91.01
Board Size	127	9.24	3.91	4	6	8	12	24
Outside Board Members (%)	127	43.84	17.31	0	33.33	42.86	57.14	85.71
Institutional Ownership (%)	127	29.92	10.65	1.02	13.52	29.05	51.38	71.25
Board Stock Ownership (%)	123	7.31	13.65	<1	<1	1.8	7.85	88.23
Market Capitalization ($ millions)	128	2432.21	8638	2.67	16.71	134.60	1398.62	77591.44

(table continued)

Panel B: Succession Details

	Number	% of Sample
Forced Departure	9	7.03%
New CEO/Chairman has served as an interim office holder before obtaining the permanent title	8	6.25%
Departing chairmen that are founders or members of the founding family	25	19.53%
Firm is listed on NYSE	64	50%
Firm is listed on NASDAQ	54	42.19%
Firm is listed on AMEX	7	5.47%

Panel C: Incoming CEO and Chairman's Origin

	Number	% of Sample
Incoming CEO is an outsider	41	32.03%
Incoming CEO was President or Chief Operating Officer	45	35.16%
Incoming CEO was President or CEO of a subsidiary	5	3.91%
Incoming CEO was Executive/Senior VP or CFO	8	6.25%
Incoming CEO was outside director or consultant to the firm	23	17.97%
Vice Chairman	4	3.13%
Retired Chairman and CEO	2	1.56%

Panel D: Departing CEO and Chairman's Future Career

	Number	% of Sample
Departing chairmen that serve on other boards after retirement	38	29.68%
Departing chairman stays on the board as Chairman Emeritus	2	1.56%
Departing chairman stays on the board as a director	51	39.84%
Departing chairman stays on the board as chairman of the executive committee	4	3.13%
Departing chairman stays on the board as a consultant to the firm	9	7.03%

The path to becoming the CEO and chairman of the board of a unitary leadership firm seems more varied than the path to the top of a firm using probationary succession process. Almost a third, 41 (32.03 %), of the new heads of unitary leadership firms are outsiders. They hold the CEO or CEO and chairmen positions in other corporations. In terms of inside succession however, 45 (35.16 %) of new CEOs are previously presidents or chief operating officers (COOs), while 23 (17.97 %) are either outside directors or consultants to the firms. Presidents or CEOs of the main subsidiaries of the firms (five

cases, 3.91 %), executive, senior vice presidents (8 cases, 6.25%) and vice chairmen (four cases, 3.13%) constitute other successors in unitary leadership firms. In two cases (1.56%) the incoming CEO and chairmen are previously retired chairmen or CEOs of the firms who are asked to step in by the board of directors and take over following an unexpected or forced departure.

The future career prospects of the departing chairmen and CEOs are also varied. Since the retirement age is higher in this sample of unitary leadership firms, the number of CEOs and chairmen that pursue further careers is also lower compared to the probationary succession sample. Still, 38 (29.68 %) of departing heads serve on the boards of directors of other firms, while 51 (39.84%) continue to serve as directors in their own firms. Two (1.56 %) of the departing CEO and chairmen stay on their own board as Chairmen Emeriti, and four (3.13%) remain as the chairmen of the executive committee. Similarly, nine (7.03 %) departing chairmen and CEOs do not remain on the board of directors but continue to serve their companies as consultants.

5.3. Succession from Dual Leadership to Dual Leadership

Dual leadership firms have separate individuals holding the CEO and chairman of the board titles. In my sample, there are 90 managerial turnover announcements by firms with dual leadership; 48 firms (53.33 %) announcing only a change of CEOs while the chairman of the board stays the same; (37.78 %) announcing only a change of chairmen while the CEO remains the same and eight firms (8.89 %) announce that they are changing both their CEOs and chairmen at the same time (See Table 5.5 Panel B). Table 5.5 presents the descriptive statistics for the entire sample of 90 dual leadership firms. Then, the different types of changes are analyzed in more detail.

Table 5.5
Dual Leadership Firms

Panel A presents the descriptive statistics of the sample of dual leadership firms that announce a managerial change between 1993 and 1995. CEO and Chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO or chairmen and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents the number of firms changing only their CEOs, those changing only their Chairmen and those changing both simultaneously as well as the exchanges the firms are listed on.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing CEO Age	90	53.36	7.86	36	48	53	58	72
Departing CEO Tenure as CEO	90	4.55	4.47	0.5	1.88	3	5.5	25
Departing CEO Prior Time with the Firm	90	10.99	10.07	0.5	4	9	13	47
Departing CEO Share Ownership (%)	90	1.98	3.34	<1	<1	0.89	2.36	20.80
Incoming CEO Age	90	50.29	6.77	37	46	51	55	77
Incoming CEO Prior Time with the Firm	90	7.10	9.62	0	0.5	3	9	47
Incoming CEO Prior Time as a director on the board	90	3.70	4.55	0	0	2	6	22
Incoming CEO Share Ownership (%)	90	0.95	1.58	<1	<1	<1	1.55	5.80
Departing Chairman Age	90	61.88	9.82	39	54	64	69	85
Departing Chairman Tenure as Chairman	90	8.46	8.17	0.5	3	6	10	38
Departing Chairman Prior Time with the Firm	90	16.21	12.70	1	6	13	22	47
Departing Chairman Share Ownership (%)	90	7.70	12.77	<1	<1	1.88	9.65	57.94
Incoming Chairman Age	90	59.59	8.83	40	53	60	67	76
Incoming Chairman Prior Time with the Firm	90	11.72	11.11	0	3	9	15	47
Incoming Chairman Prior Time as a director on the board	90	11.25	11.13	0	3	8	14	47
Incoming Chairman Share Ownership (%)	90	5.87	11.45	<1	<1	1.20	5.03	57.94
Board Size	90	8.02	2.67	3	6	7	9	18
Outside Board Members (%)	90	31.41	13.05	0	22.92	33.33	40	58.33
Institutional Ownership (%)	90	41.05	13.54	2.65	14.81	39.47	55.16	91.03
Board Stock Ownership (%)	90	6.58	8.42	<1	1.47	3.60	8.29	51
Market Capitalization ($ millions)	90	435.24	967.45	0.35	19.05	70.39	325.74	5114.62

(table continued)

Panel B: Succession Details

	Number	% of Sample
Changing only their CEOs while the Chairman remains in office	34	37.78 %
Changing only their Chairmen while the CEO remains in office	48	53.33 %
Changing both their CEOs and Chairmen simultaneously	8	8.88 %
Firm is listed on NYSE	35	38.88 %
Firm is listed on NASDAQ	42	46.67 %
Firm is listed on AMEX	8	8.88 %

The departing chairmen of the board are on average (median) 61.88 (64) years old with an average (median) of 8.46 (6) years of tenure as chairmen, and an average (median) of 16.21 (13) years of service to the firm as an employee. Departing CEOs on the other hand, are on average (median) 53.36 (53) years old with an average (median) of 4.55 (3) years of tenure as CEOs during their on average (median) 10.99 (9) years of time spent working for the firm. Similarly, departing chairmen own on average (median) 7.70% (1.88%) stock in the firm, whereas departing CEOs own only 1.98% (0.98%) on average (median).

Incoming chairmen are on average (median) 59.59 (60) years old with an average (median) of 11.72 (9) years of service in the firm, on average (median) 11.25 (8) of those spent as directors in the board. Incoming CEOs, meanwhile, are on average (median) 50.29 (51) years old with an average (median) of 7.10 (3) years of service to the firm, on average (median) 3.70 (2) of those years spent of the board of directors. Incoming chairmen own on average (median) 5.87% (1.20%) stock in the firm, while the incoming CEOs own on average (median) only 0.95% (less than 1%) of the shares of the firm.

Firms with dual leadership structures that announce a managerial change have on average (median) 8.02 (7) directors on their board, an average (median) of 31.41% (33.33%) of whom are outsiders. The directors on the board except for the incumbent

CEO and Chairman own on average (median) 6.58% (3.60%) of the equity in the firm, while institutional investors hold on average (median) 41.05% (39.47%) ownership in these firms.

Dual leadership firms tend to be smaller in market capitalization compared to others. The average (median) size of the dual leadership firms in my sample is $435.24 million ($70.39 million) in terms of market capitalization. Of the 90 dual leadership firms in my sample, 35 (38.88%) of these firms trade on the NYSE, while 42 (46.67%) trade on NASDAQ and 8 (8.88%) trade on AMEX.

5.3.1. Dual Leadership Firms that Change Only Their CEOs While Their Chairmen Remain the Same

There are 46 firms in my sample that have separate CEO and chairman of the board titles and between 1993 and 1995 announce that they are changing their CEOs, while their chairmen remain the same. Two additional firms that do not have chairmen of the board are also included in this sample. The highest office in the company is the CEO. Table 5.6 presents the descriptive statistics on these firms and the origins of their new CEOs as well as the future careers of their departing CEOs.

The chairmen of these firms are on average (median) 61 (62.5) years old with an average (median) of 6.5 (4) year tenure as the chairmen of their firms. During their average (median) 14.74 (11) years time spent in their companies, these chairmen have accumulated on average (median) 9.54% (2.41%) of the shares of the firm. The maximum share ownership of 57.94 % of the stock of the firm belongs to 74-year old Leonard J. Bruce, who has been chairman of the board at Vallen Corporation for 34 years and has been with the company for over 47. Except for this outlier, the maximum share ownership by chairmen is 25 %.

Table 5.6
Dual to Dual Succession: Firms that Change Only Their CEOs

Panel A presents the descriptive statistics of the dual leadership sample that change only their CEOs while the chairman of the board stays in office. CEO and chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and Chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and chairman and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents certain firm characteristics like the exchanges the firms are listed on, the number of new CEO/Chairman that served as interim office holders before being granted the permanent title, the number of founders and members of the founding family that are relinquishing their titles. Panels C and D present the origins of incoming CEOs and the future career choices of departing CEOs, respectively.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing CEO Age	42	54.88	9.10	36	48.25	55.5	61.75	72
Departing CEO Tenure as CEO	41	5.34	5.13	1	2	4	6	25
Departing CEO Prior Time with the Firm	41	15.02	12.11	2	6	10	25	47
Departing CEO Share Ownership (%)	46	1.82	3.49	<1	<1	0.22	2.27	20.80
Incoming CEO Age	48	50.77	7.58	37	45	50.5	56	77
Incoming CEO Prior Time with the Firm	48	8.29	12.05	0	0	3	15	47
Incoming CEO Prior Time as a director on the board	48	2.38	3.40	0	0	0.625	4	12
Incoming CEO Share Ownership (%)	48	0.60	1.37	<1	<1	<1	0.05	5
Chairman Age	46	61.04	9.44	40	54	62.5	69	76
Chairman Tenure as Chairman	46	6.51	6.89	1	3	4	7.75	34
Chairman Prior Time with the Firm	46	14.74	12.11	1	5.25	11	20.25	47
Chairman Share ownership (%)	46	9.54	14.64	<1	<1	2.41	13.5	57.94
Board Size	48	8	2.87	3	6	7	9	18
Outside Board Members (%)	48	29.70	12.69	0	21.67	30.38	36.88	58.33
Institutional Ownership (%)	48	39.87	11.24	2.65	11.37	37.12	51.76	78.16
Board Stock Ownership (%)	48	7.45	10.62	<1	0.90	3.2	8.23	51
Market Capitalization ($ millions)	48	450.61	924.89	0.97	21.18	91.92	340.61	4200.43

(table continued)

Panel B: Succession Details

	Number	% of Sample
Forced Departure	3	6.25 %
Firm has no chairman of the board; highest office is CEO	2	4.17 %
Departing chairmen that are founders or members of the founding family	3	6.25 %
Firm is listed on NYSE	19	39.58 %
Firm is listed on NASDAQ	20	41.67 %
Firm is listed on AMEX	6	12.50 %

Panel C: Incoming CEO's Origin

	Number	% of Sample
Incoming CEO is an outsider	18	37.50 %
Incoming CEO was President or Chief Operating Officer	13	27.08 %
Incoming CEO was President or CEO of a subsidiary	4	8.33 %
Incoming CEO was Executive/Senior VP or CFO	9	18.75 %
Incoming CEO was outside director or consultant to the firm	4	8.33 %

Panel D: Departing CEO's Future Career

	Number	% of Sample
Departing CEO stays on the board as a director	11	22.92 %
Departing CEO becomes vice chairmen	4	8.33 %

The departing CEOs of dual leadership firms that change only their CEOs are on average (median) 54.88 (55.5) years old with an average (median) of 15.02 (10) years of service to their companies, on average (median) 5.34 (4) years of which have been as the CEO. Their average (median) stock ownership in the firm is 1.82 % (0.22 %), significantly lower than the ownership of the chairmen. The maximum share ownership in departing CEOs is 20.80% of Zonic Corp's shares owned by Gerald Zobrist. Zonic Corp, however, is one of the two companies that do not have a chairman of the board, and the highest corporate office is the office of the chief executive officer. Excluding that outlier, there are no companies in my sample with over 5% share ownership by their departing CEOs. Of these departing CEOs, only four (8.33 %) become vice chairmen of

the board, later to succeed the current chairmen, whereas 11 (22.92 %) remain on the board as directors.

Incoming CEOs, on the other hand, are on average (median) 50.77 (50.5) years old and have been with their companies on average (median) 8.29 (3) years, with an average (median) 2.38 (0.625) years of that time spent as directors. Both the mean and median share ownership of the incoming CEOs is less than 1% of the shares of the firm. More than a third of the incoming CEOs are from other companies (18 cases, 37.50 %). On the other hand, 13 (27.08%) of the new CEOs were previously presidents or chief operating officers of their companies, and 9 (18.75%) have been executive or senior vice presidents. Four (8.33%) of the incoming CEOs were heads of a subsidiary and another 4 (8.33%) were outside directors or consultants to their firms.

The boards of directors in these firms are made up of an average (median) of 8 (7) members, on average (median) 29.70 % (30.38%) of whom are outsiders. The members of the board except for the chairman and the CEO, own on average (median) 7.45% (3.2%) of the stock of the firm, whereas institutional investors own on average (median) 39.87% (37.12%) of the shares in these firms. Only 2 of the departing CEOs have been forced to leave, and only 3 of the departing CEOs are founders of the firms or members of the founding family.

The average (median) size of the dual leadership firms that change only their CEOs while their chairmen remain the same is $ 450.61 million ($91.92 million). Of the 48 dual leadership firms changing only their CEOs, 19 (39.58 %) trade on the NYSE, while 20 (41.67 %) and 6 (12.50 %) trade on NASDAQ and the AMEX, respectively.

5.3.2. Dual Leadership Firms that Change Only Their Chairmen While Their CEOs Remain the Same

In my sample there are 34 dual leadership firms that change only their chairmen while their CEOs remain in office. Table 5.7 presents the descriptive statistics and the succession details on these firms. The CEOs of these firms are on average (median) 50.47 (51) years old and have an average (median) tenure of 2.99 (1.88) years as the CEO of their respective firms. They have been with their firms on average (median) 6.18 (4.5) years and own on average (median) 1.55 % (0.95 %) of their company's stock. The CEOs in this sub-sample have significantly less tenure than their counterparts in the firms engaging in other types of succession processes presented above. However, this is mainly because the tenure of the CEOs in this sample remains yet to be concluded.

The departing chairmen are on average (median) 62.16 (64) years old and have served their corporations for an average (median) of 18.03 (13) years, an average (median) 11.15 (8) years of which as chairmen of the board of directors. They own on average (median) 6.27 % (1.4%) of their companies' stock. The oldest chairman to leave his office during this time period is 85-years-old Frank Stanton of Broadcast International Inc, and was replaced by the 69 years-old consultant to the company, Howard G. Haas. The CEO of Broadcast International during this time and for another five years after the chairman succession was the 39-years-old Dwight G. Egan. Similarly, J.B Hunt, the founder of J.B. Hunt Transportation Services owned 39.9 % of the stock of his company when he retired at the age of 68 to be replaced by the 42 years-old Wayne Garrison, who had been with the company for over 22 years. Except for J.B. Hunt, the maximum share ownership by a departing chairman was 12.52 %.

Table 5.7
Dual to Dual Succession: Firms that Change Only Their Chairmen

Panel A presents the descriptive statistics of the dual leadership sample that change only their chairmen while the CEO stays in office. CEO and chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and Chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and chairman and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming chairman of the board and the CEO. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents certain firm characteristics like the exchanges the firms are listed on, the number of founders and members of the founding family that are relinquishing their titles. Panels C and D present the origins of incoming chairmen and the future career choices of departing chairmen, respectively.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing Chairman Age	31	62.16	11.11	39	54	64	69.5	85
Departing Chairman Tenure as Chairman	31	11.15	9.74	0.5	4	8	14.5	38
Departing Chairman Prior Time with the Firm	31	18.03	12.96	2	6.5	13	25.5	46
Departing Chairman Share Ownership (%)	32	6.27	10.87	<1	<1	1.4	5.27	39.9
Incoming Chairman Age	34	58.71	8.25	42	51.25	58.5	64.5	76
Incoming Chairman Prior Time with the Firm	34	8.06	9.58	0	2	4	10.75	38
Incoming Chairman Prior Time as a director on the board	34	7.09	9.25	0	1.25	3	9.75	38
Incoming Chairman Share Ownership (%)	34	0.98	1.76	<1	<1	<1	1.45	6.15
CEO Age	34	50.47	5.41	39	47	51	55	60
CEO Tenure as CEO	34	2.99	2.82	0.5	1	1.88	4	11
CEO Prior Time with the Firm	34	6.18	5.28	0.5	2.25	4.5	9	22
CEO Share ownership (%)	34	1.55	1.80	<1	<1	0.94	2.3	5.8
Board Size	34	8.15	2.34	5	6	8	9.75	14
Outside Board Members (%)	34	33.33	13.02	0	24.73	33.33	42.86	54.55
Institutional Ownership (%)	34	40.78	12.57	3.29	16.57	38.91	58.39	87.45
Board Stock Ownership (%)	34	5.86	4.96	<1	2.52	4.86	8.54	19.84
Market Capitalization ($ millions)	34	295.68	748.78	0.35	18.10	48.12	253.23	4287.65

Panel B: Succession Details

	Number	% of Sample
Forced Departure	2	5.88 %
Succession is the result of the death of the departing chairman	3	8.82 %
Departing chairmen that are founders or members of the founding family	8	23.53 %
Firm is listed on NYSE	13	38.24 %
Firm is listed on NASDAQ	17	50.00 %
Firm is listed on AMEX	2	5.88 %

(table continued)

Panel C: Incoming Chairmen's Origin

	Number	% of Sample
Incoming Chairman is an outsider	1	2.94 %
Incoming Chairman was President or Chairman of a subsidiary	1	2.94 %
Incoming Chairman was Executive/Senior VP or CFO	5	14.71 %
Incoming Chairman was outside director or consultant to the firm	25	73.53 %

Panel D: Departing Chairmen's Future Career

	Number	% of Sample
Departing chairmen that serve on other boards after retirement	11	32.35 %
Departing chairman stays on the board as Chairman Emeritus	4	11.76 %
Departing Chairman stays on the board as a director	10	29.41 %

Incoming chairmen, on the other hand, are on average (median) 58.71 (58.5) years old with on average (median) 8.06 (4) years of prior time in the company, on average (median) 7.09 (3) years of which are as directors on the board. The incoming chairmen own, on both average and median, less than 1% stock ownership in the firms. Most of the incoming chairmen have long experiences on boards; 25 out of the 34 in this sample (73.53%) were either outside directors with a long tenure on the board of the company or long-time consultants to the firm. Apart from these, there was only one case where the new chairmen was a complete outsider, having never served on the board of the company before. Five (14.71 %) of the incoming chairmen were previously senior or executive vice presidents or CFOs, and one (2.94 %) was the CEO of a subsidiary of the firm.

Most of the departing chairmen seem to stay on the boards of their own company or other companies after retirement. Of the 34 cases in my sub-sample, 11 (32.35%) departing chairmen continue their careers as directors on the boards of other companies, while 10 (29.41 %) remain on the boards of their own companies as director. Meanwhile, 4 (11.76 %) departing chairmen continue their services to their company as Chairmen Emeriti.

The boards of directors of dual leadership firms that change only their chairmen have an average (median) of 8.15 (8) members on their boards and a third (both on average and median) of these directors are outsiders. The size of the board and the percentage of outsiders is similar to the general dual leadership firm in this sample as well as to those that change only their CEOs. The members of the board that are not chairmen or CEOs, own on average (median) 5.86 % (4.86 %) of the shares of the company. The median board share ownership in dual leadership firms that change their CEOs are significantly higher than the board ownership in other dual leadership firms. This may imply that it takes a higher level of stock based incentives for board members to act in the interests of shareholders and not under the influence of the chairmen or the CEO. Additionally, literature suggests that around at least 5% ownership is required to properly align the incentives of managers and shareholders and solve the Jensen and Meckling (1976) agency problem implicitly.

Moreover, firms that have dual leadership structures seem to experience a more rapid turnover in CEOs compared to chairmen. The firms that change their CEOs and those that change their chairmen are very similar in my sample. However, the average CEO turnover in these firms seems to be twice as much. Both the average and the median tenure of departing chairmen are twice as much as those of departing CEOs. Similarly, departing chairmen own significantly more stock in their firms than departing CEOs do. This indicates that departing chairmen may be more entrenched to their firms than CEOs would be.

There are only two cases (5.88 %) of forced departure of chairmen in my sample of dual leadership firms that change only their chairmen, and only three cases (8.82 %)

where succession was the result of the death of the former chairman. Eight departing chairmen (23.53 %) are founders or members of the founding families of these firms.

The mean (median) size of the firms in this sample is $ 295.68 million ($48.12 million), and the distribution between the exchanges for the firms in this sub-sample are as follows: 13 (38.24 %) trade on the NYSE, while half (17 firms) trade on NASDAQ and 2 (5.88 %) trade on the AMEX. Institutional ownership in these firms is on average (median) 40.78 % (38.91%).

5.3.3. Dual Leadership Firms that Change Both Their CEOs and Chairmen of the Board at the Same Time

There are only 8 firms in my sample that have dual leadership structures, in other words, have separate individuals holding the Chairman of the board and CEO titles, and that change both of these individuals simultaneously (Table 5.8). However, 6 (75%) of these cases are actually passing-the-baton type cases. In these cases, the incumbent Chairman of the board leaves his chair to the current CEO of the firm, while the incumbent CEO resigns his post to his heir apparent, usually the president or COO of the company, to take the Chairman position. These processes are very similar to probationary succession processes following a relay-race style procedure. However, none of the individual managers obtain a combined CEO and Chairman of the board title at any point of their career.

Though with a small sample size like 8, it is very difficult to make statistically significant statements, the age and tenure characteristics of the departing chairmen in these firms are very similar to the firms in my probationary succession process sub-sample. The departing chairmen in this sample are on average (median) 62.63 (66.5)

years old, with an average (median) tenure of 9.25 (9.50) years as chairmen and an average (median) of 17.63 (12.5) years as employees of the firms they are leaving. They own on average (median) 2.89% (0.75%) of the shares in the firms they are retiring from. The minimum age for a departing chairman is 56, George A Castrucci of Baldwin Piano and Organ Co., suggesting that these departing chairmen are mostly at their retiring age and are passing-the-baton to their CEOs. These characteristics are consistent with Vancil's (1987) description of relay-race type succession processes. Out of the 8 departing chairmen 3 (37.50%) remain on the board of their companies as directors, while another 3 (37.50%) remain as Chairmen Emeriti. Thus, most of the incentive conflicts that exist in probationary processes also exist for these firms.

The incoming chairmen are on average (median) 55 (56) years old, and have an average (median) of 9.88 (10) years of experience in the company, on average (median) 8.88 (8) years of which has been as directors on the boards of their firms. These incoming chairmen own on average (median) 5.55% (3.45%) stock in their firms.

Six out of these 8 incoming chairmen are departing CEOs of their firms. Therefore, the descriptive statistics of departing CEOs are very similar to those of incoming chairmen. The departing CEOs in these firms are on average (median) 57.63 (57) years old, with an average (median) tenure of 7.13 (6) years as CEOs of their firms, and an average (median) of 10.75 (10.5) years of prior service to the company. The departing CEOs hold on average (median) 4.67% (2.55%) stock ownership in their firms.

Table 5.8
Dual Leadership Firms: Firms that Change Both Their Chairmen and CEOs

Panel A presents the descriptive statistics of the sample of dual leadership firms that announce a managerial change between 1993 and 1995. CEO and Chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO or chairmen and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents the number of firms changing only their CEOs, those changing only their Chairmen and those changing both simultaneously as well as the exchanges the firms are listed on.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing Chairman Age	8	65.63	5.93	56	62.25	66.5	69.25	74
Departing Chairman Tenure as Chairman	8	9.25	5.50	1	6.25	9.5	12.25	18
Departing Chairman Prior Time with the Firm	8	17.63	15.57	2	7.75	12.5	23.75	42
Departing Chairman Share Ownership (%)	8	2.89	4.59	<1	<1	0.75	3.23	12.7
Incoming Chairman Age	8	55	5.86	46	51.75	56	58.25	62
Incoming Chairman Prior Time with the Firm	8	9.88	5.54	0	7	10	13	17
Incoming Chairman Prior Time as a director on the board	8	8.88	4.96	0	7	8	12	17
Incoming Chairman Share Ownership (%)	8	5.55	5.67	<1	1.80	3.45	8.00	16.5
Departing CEO Age	8	57.63	5.80	48	54.5	57	62.5	65
Departing CEO Tenure as CEO	8	7.13	4.85	2	4.25	6	9	16
Departing CEO Prior Time with the Firm	8	10.75	3.54	7	7.75	10.5	12.75	16
Departing CEO Share Ownership (%)	8	4.67	5.95	<1	0.68	2.55	5.67	16.5
Incoming CEO Age	8	46.14	6.31	38	42	47	49.5	55
Incoming CEO Prior Time with the Firm	8	3.36	5.85	0	0	1	3.25	16
Incoming CEO Prior Time as a director on the board	8	0.71	0.95	0	0	0	1.5	2
Incoming CEO Share Ownership (%)	8	0.58	1.09	<1	<1	<1	0.48	2.9
Board Size	8	7.63	2.97	4	5.75	7	9	12
Outside Board Members (%)	8	35.80	16.23	0	32.14	40.83	44.64	50
Institutional Ownership (%)	8	40.55	12.37	2.89	15.21	39.12	56.41	91.03
Board Stock Ownership (%)	8	4.49	3.89	<1	1.54	3.70	7.90	10
Market Capitalization ($ millions)	8	936.16	1769.27	0.67	34.57	73.13	876.43	5114.62

(table continued)

Panel B: Succession Details

	Number	% of Sample
Passing-the-baton type succession processes	6	75%
Departing chairman is the founder or member of the founding family	1	12.50%
Firm is listed on NYSE	3	37.50%
Firm is listed on NASDAQ	5	62.50%
Firm is listed on AMEX	0	0

Panel C: Incoming CEO's Origin

	Number	% of Sample
Incoming Chairman is an outsider	3	37.50%
Incoming Chairman was COO	1	12.50%
Incoming Chairman was Executive/Senior VP or CFO	3	37.50%
Incoming Chairman was outside director or consultant to the firm	1	12.50%

Panel D: Departing Chairmen's Future Career

	Number	% of Sample
Departing chairman stays on the board as Chairman Emeritus	3	37.50%
Departing Chairman stays on the board as a director	3	37.50 %
Steps down to be vice-chairman	1	12.50%

Incoming CEOs, on the other hand, are on average (median) 46.14 (47) years old. They have an average (median) of only 3.36 (1) years of experience in the company, and more than half have never served on the boards of their corporations. They own less than 1% stock in the firms both on average and median. Three (37.50%) out of the 8 incoming CEOs in this sample are outsiders, while another 3 (37.50%) are promoted from executive vice presidents, and one (12.50%) new CEO is the incumbent COO of the firm.

Dual leadership firms that simultaneously change both the CEOs and their Chairmen have average (median) market capitalizations of $ 936.16 million ($73.13 million). Three out of the 8 firms (37.50%) trade on the NYSE while 5 (62.50%) trade

on NASDAQ. There are on average (median) 7.63 (7) people on the board of directors in these firms and on average (median) 35.80% (40.83%) of the directors are outsiders. Directors except the incumbent Chairmen and CEOs own on average (median) 4.49 % (3.70%) stock in these firms while institutional investors own on average (median) 40.55% (39.12%).

5.4. Firms that Move from Unitary to Dual Leadership Structures: Separation of Chairman of the Board and CEO Titles

There are 38 firms in my sample that have unitary leadership structures, but decide to separate their Chairman of the board and CEO titles. Table 5.9 presents the descriptive statistics on these companies as well as the details of their succession processes. Seventeen (44.74%) of these cases are incomplete passing-the-baton cases, where the individual holding the combined CEO/Chairman of the board title relinquishes his CEO title to the heir apparent, and stays on as the chairman of the board. Normally, after a probationary period, during which the departing CEO, incumbent chairman, and the new CEO serve the company together, the new CEO gets awarded the combined title of CEO and Chairman of the board. At this point, the old chairman leaves the chairman position to pursue his career. In these incomplete passing-the-baton cases, however, the probationary period is still in progress at the end of year 2002. Therefore, the companies have separate Chairman and CEOs. Since there is no way to tell when the probationary period will end, and whether the new CEO will be awarded the combined title, I have classified these cases under separation of titles. Furthermore, in most of these cases, the probationary periods are at least 6 to 7 years, (significantly lager than the average of 2.46 years in probationary succession processes, with a t-statistic of 3.15 and a p-

value<0.0001), which shows that these firms are effectively run with dual leaders for s significant amount of time to be treated separately from probationary processes.

Table 5.9
Separation of Titles: Firms that Move from Unitary to Dual Leadership

Panel A presents the descriptive statistics of the sample of dual leadership firms that announce a managerial change between 1993 and 1995. CEO and Chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO or chairmen and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents the number of firms changing only their CEOs, those changing only their Chairmen and those changing both simultaneously as well as the exchanges the firms are listed on.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing Chairman and CEO Age	38	58.64	9.65	42	50	62	65	76
Departing Chairman and CEO Tenure as Chairman	38	9.56	9.56	1	3	6.5	11.75	39
Departing Chairman and CEO Tenure as CEO	38	12.85	10.45	1	4	10	20	39
Departing Chairman and CEO Prior Time with the Firm	38	17.74	12.52	3	8	13.5	28.75	45
Departing Chairman and CEO Share Ownership (%)	38	9.10	10.62	<1	1.44	4.20	12.95	33.60
Incoming Chairman Age	38	58.14	9.78	40	51	60	65	76
Incoming Chairman Prior Time with the Firm	38	16.95	13.60	0	7	11.5	26.75	45
Incoming Chairman Prior Time as a director on the board	38	14.79	12.26	0	5.5	11	23.5	41
Incoming Chairman Share Ownership (%)	38	10.26	15.48	<1	<1	3.48	13.23	71.70
Incoming CEO Age	38	49.70	6.91	37	46	50	54	66
Incoming CEO Prior Time with the Firm	38	6.83	8.38	0	0.25	3.5	10	31
Incoming CEO Prior Time as a director on the board	38	4.09	6.21	0	0	2	4.75	31
Incoming CEO Share Ownership (%)	38	1.93	4.52	0	<1	<1	1.92	24.80
Board Size	38	8	2.60	3	6	8	9	14
Outside Board Members (%)	38	28.78	11.92	0	20.56	28.57	37.50	57.14
Institutional Ownership (%)	38	32.59	13.72	0.94	12.51	33.28	51.37	76.27
Board Stock Ownership (%)	38	7.50	8.25	<1	2.68	5.77	9.39	36.60
Market Capitalization ($ millions)	38	293.91	544.27	1.08	30.97	91.71	375.12	2988.75

(table continued)

Panel B: Succession Details

	Number	% of Sample
Incomplete Passing-the-baton type successions	17	44.74%
Changes only their CEO	19	50.00%
Changes only their chairmen	2	5.26%
Changes both the chairman and the CEO at the same time	18	47.37%
Departing chairman or CEO is the founder or member of the founding family	13	34.21%
Firm is listed on NYSE	15	39.47%
Firm is listed on NASDAQ	16	42.11%
Firm is listed on AMEX	6	15.79%

Panel C: Incoming Chairman or CEO's Origin

	Number	% of Sample
Incoming Chairman is an outsider	6	15.79%
Incoming CEO is an outsider	10	26.32%
Incoming CEO is the president or COO of the company	17	44.74%

The mean (median) age of departing chairmen and CEOs in this sample is 58.64 (62). The departing chairmen and CEOs have served on average (median) 9.56 (6.5) years as chairmen and 12.85 (10) years as CEOs of their companies. They have been employed by their companies on average (median) 17.74 (13.5) years when they leave their positions, and own on average (median) 9.10% (12.95%) stock in their firms. The youngest chairmen and CEO to leave his position is 42-years-old Oliver Richard III, who left New Jersey Resources as chairman and CEO to take a similar position in Columbia Gas Co. He was replaced as chairman of the board by one of the outside directors of the company, Bruce G. Coe, and as CEO by Lawrence M Downes, the senior vice president and Chief Financial Officer of the company.

The incoming chairmen are on average (median) 58.14 (60) years old and have been with the company on average (median) 16.95 (11.5) years, an average (median) of 14.79 (11) of which have been as directors on the board. The incoming chairmen own on

average (median) 10.26% (3.48%) stock in the firms. The high average stock ownership is the result of 71.70% stock ownership of Sam Zell, who steps up as the chairman of Carter Hawley Hale Stores after the founder and 17-years-long chairman, Phillip P. Hawley retires. Sam Zell's personal fund owns 71.70% of the shares in Carter Hawley Hale Stores, and as the controlling shareholder, he took the chairman position after the retirement of the founder.

Meanwhile, incoming CEOs are on average (median) 49.70 (50) years old and have served an average (median) of 6.83 (3.5) years in their companies, and average (median) of 4.09 (2) years of which are as directors on the board. The equity ownership of incoming CEOs is on average 1.93% and the median is less than 1 %.

Of the 38 firms that separate their chairman on the board and CEO titles, 19 (50%) do so by changing only their CEO and keeping their chairman in position, whereas only 2 (5.26%) change only their chairman, keeping their CEO in position. The remaining 18 firms (47.37%) separate their titles when the executive holding the combined CEO/Chairman of the board title leaves and is replaced by two separate individuals for the respective positions.

Separation of titles seems to be prevalent when members of the founding family leave governing positions in the firms to non-family members. In 13 (34.21%) of the cases in my sample, the departing CEO and Chairman is either the founder of the firm or a member of the founding family.

The origins of the newcomers in title separations are not as varied as other forms of succession. In 17 cases out of 38 (44.74%), the new CEO is either the president or the

chief operating officer (COO) of the firm. In another 10 cases, the new CEO is an outsider and in 6 cases, the incoming chairman is an outsider as well.

The firms in this sub-sample that move from unitary to dual leadership structures have on average (median) $293.91 million ($91.71 million) of size in market capitalization. Their average (median) board size is 8 (8) directors, 28.78% (28.57%) of which are outside directors on average (median). Stock ownership of board members other than the CEO or the chairman is 7.50% (5.77%) on average (median), while institutional ownership of equity in these firms is on average (median) 32.59% (33.28%). Of the 38 firms included 15 (39.47%) trade on the NYSE, while 16 (42.11%) and 6 (15.79%) trade on NASDAQ and AMEX respectively.

5.5. Firms that Move from Dual to Unitary Leadership Structures: Unification of Chairman of the Board and CEO Titles

My sample of managerial successions between years 1993 and 1995 includes 14 cases where dual leadership firms have combined their CEO and chairman of the board titles. Table 5.10 presents the descriptive statistics and succession details on these cases. In 6 of these cases (42.86% of the sample) the incumbent chairman takes on the title of CEO as well, after the current CEO leaves the firm, while in another 4 cases (28.57%) the reverse happens and the CEO takes over the chairman office as well. In the remaining 4 cases (28.57%) both the CEO and the chairman are replaces by a third party holding the combined title.

The departing chairmen in this sample are on average (median) 56.54 (61) years old and have an average (median) tenure of 7.33 (5) years as chairmen of their boards. They have been employees of their firms on average (median) 14.38 (11) years and hold on average (median) 5.04% (2.70%) stock ownership in the firm.

Table 5.10
Unification of Titles: Firms that Move from Dual to Unitary Leadership

Panel A presents the descriptive statistics of the sample of dual leadership firms that announce a managerial change between 1993 and 1995. CEO and Chairman ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO or chairmen and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. Panel B presents the number of firms changing only their CEOs, those changing only their Chairmen and those changing both simultaneously as well as the exchanges the firms are listed on.

Panel A: Descriptive Statistics

Variable	N	Mean	Std Dev	Min	25%	Median	75%	Max
Departing Chairman Age	8	56.54	8.13	44	49	61	63	66
Departing Chairman Tenure as Chairman	8	7.33	6.26	2	3	5	8	21
Departing Chairman Prior Time with the Firm	8	14.38	12.76	3	5	11	21	43
Departing Chairman Share Ownership (%)	8	5.04	6.49	<1	1.00	2.70	7.38	23.30
Departing CEO Age	10	49.92	8.99	36	43.75	50	53.25	67
Departing CEO Tenure as CEO	10	6.68	5.24	2	3	5	8.25	18
Departing CEO Prior Time with the Firm	10	12.04	9.59	3	5.75	7.25	15	31
Departing CEO Share Ownership (%)	10	4.35	6.19	<1	<1	1.90	5.50	22.30
Incoming Chairman and CEO Age	14	50.36	6.88	36	46.5	51	53.5	63
Incoming Chairman and CEO Prior Time with the Firm	14	9.78	8.55	0	4	7	13.25	30
Incoming Chairman and CEO Prior Time as a director on the board	14	9.21	8.27	0	4	6.5	13.5	28
Incoming Chairman and CEO Share Ownership (%)	14	6.30	7.66	0	0.25	4.65	8.10	23.30
Board Size	14	8.29	2.58	5	6.5	8	8.75	14
Outside Board Members (%)	14	34.31	16.48	12.50	23.56	33.33	39.38	71.43
Institutional Ownership (%)	14	31.52	14.38	2.11	12.67	32.41	53.19	78.34
Board Stock Ownership (%)	14	7.64	9.00	<1	2.13	4.40	11.10	31.80
Market Capitalization ($ millions)	14	2347.96	5199.49	1.13	23.22	65.21	856.57	14635.31

(table continued)

Panel B: Succession Details

	Number	% of Sample
Incumbent Chairman takes over the CEO office as well	6	42.86%
Incumbent CEO takes over the Chairman office as well	4	28.57%
Both the CEO and the Chairman are replaced by a third party holding the combined title	4	28.57%
Departing chairman or CEO is the founder or member of the founding family	2	14.29%
Incoming Chairman and CEO is the founder or member of the founding family	4	28.57%
Departing Chairman or CEO remains on the board	4	28.57%
Firm is listed on NYSE	6	42.86%
Firm is listed on NASDAQ	8	57.14%
Firm is listed on AMEX	0	0%

The departing CEOs, on the other hand, are on average (median) 49.92 (50) years old with an average (median) tenure of 6.68 (5) years as CEOs of the firm and average (median) of 12.04 (7.25) years of work experience in the company. Their stock holdings are on average (median) 4.35% (1.90%).

The incoming CEO and chairman that will hold the new combined title have an average (median) age of 50.36 (51). They have been on the boards of these companies on average (median) 9.21 (6.5) years and have further been employees of the firm for an average (median) of 9.78 (7) years. They own on average (median) 6.30% (4.65%) stock in the firm.

Except for Oracle Corp, with its $14,635.31 million market capitalization, most of the firms in this sub-sample are relatively small, with a median market capitalization of $65.21 million. They have on average (median) 8.29 (8) directors on their board, on average (median) 34.21% (33.33%) of which are outsiders. Institutional investors hold on average (median) 31.52% (32.41%) of stock ownership in these firms, while the board of directors except for the incumbent CEO and Chairman holds on average (median) 7.64% (4.40%) of the firm's stock. Six out of the 14 (42.86%) firms in this sample trade on NYSE, while the remaining 8 (44.44%) trade on NASDAQ.

There are only 2 cases (14.29%) where the departing CEO or chairmen is the founder of the firm or a member of the founding family. However, there are 4 cases (28.57%) where the incoming CEO or chairman is a founder or member of the founding family. These seem like cases where the founders feel the need to come back and take control of their companies after they have been away for a while. Similarly, in 4 cases (28.57%), the departing CEO or chairman remains on the board as a director.

The overall descriptive statistics of the sample support the findings in Brickley, Coles and Jarrell (1997). The departing CEOs of firms with dual leadership on average tend to be younger with shorter tenures and lower percentages of share ownership. The average descriptive statistics of the probationary succession sample are very similar to the overall sample. The average age of a departing chairman, for instance, in the overall sample is 60.21 while this number is 60.46 in the probationary succession sample. The average tenure and stock ownership of the departing and incoming CEOs of the firms following probationary succession processes is also similar to the overall sample. This supports Vancil's (1987) argument that probationary succession processes are the common means of managerial succession for U.S. firms.

CHAPTER 6
DOES MANAGERIAL CONFORMISM EXIST? UNIVARIATE TEST RESULTS

This chapter provides univariate test results on the operating performance and other characteristics of the companies that go through probationary succession processes and tries to see whether there is evidence of managerial conformism in these firms. It also tries to answer the question whether managerial conformism is detrimental to all firms.

6.1. Existence of Managerial Conformism and Agency Costs During the Probationary Period

Consistent with my hypotheses 1 and 2 (H_1 and H_2) stated in Chapter 3, if managerial conformism exists in firms with probationary succession processes, then there should be no significant change in the operating performance of the firm during the probationary period when the former CEO (current chairman) and the new CEO serve together. However, when the probationary period is over and the new CEO gets awarded the combined title of CEO and chairman of the board, I expect operating performance of these firms to increase significantly. Since the market would be able to foresee these effects, I expect a similar reaction in the stock returns of the firms.

Table 6.1 presents the operating performance of the firms in my sample during the time of the former CEO, during the probationary transition period and after the new CEO has obtained the chairman title as well. Three year time periods are used as the basis for comparison following Gabarro (1987) and Khurana and Nohria (2001). The changes between each period have been measured. I use return on assets (ROA) and industry

adjusted ROA (IAROA) to measure operating performance in this table,[15] following Baliga et al (1996) and Brickley, Linck and Coles (1999). Return on assets is the average [median] return on assets over these periods, calculated as the net income divided by average assets. Following Parrino (1997) and Naveen (2003), industry adjusted return on assets have been defined as the average [median] annual returns on assets net of the industry mean, where the industry is determined according to two-digit SIC codes.[16] I also use the Barber and Lyon (1997) criteria to create matched samples of firms, and report both results in separate panels.

Results presented in all three panels of Table 6.1 are consistent with expectations. Consistent with hypotheses 1 and 2 (H_1 and H_2), there are no significant changes in the accounting performance of the firms during the probationary period. However, after the completion of the probationary period, when the new CEO obtains the combined title, there is a significant increase in the operating performance of the firms using probationary succession processes. The average annual return on assets of the 183 firms that successfully complete their probationary succession processes increase by 1.93% (t-statistic = 2.97), while the average annual industry adjusted and matched sample ROAs increase by 1.26% and 1.37% respectively (with t-statistics of 2.85 and 2.91 respectively). The results are the same using medians as well.

[15] Other measures of operating performance, like return on capital following (Brickley, Coles and Jarrell (1997), return on equity (ROE) and return on investment (ROI) have been considered. However, statistical tests have revealed qualitatively the same results using all four measurements, therefore only ROAs have been reported.

[16] The industry-adjusted operating performance and market reaction variables are also calculated using four-digit SIC codes and the results are similar. Therefore, to be consistent with previous literature, two-digit SIC code based results are reported.

Table 6.1
Accounting Operating Performance of Firms with Probationary Successions

Operating performance is measured by Return on Assets, Industry Adjusted ROA and matched sample ROA. Former CEO refers to the last three years of the former CEO's tenure before the succession took place. Probationary period refers to the transition period when the former CEO/current Chairman worked together with the new CEO, and the combined period refers to the first three years of the new CEO's tenure after he obtains the combined CEO and Chairman of the Board title. Δ_F presents the mean[median] difference between the ROA and the IAROA before the former CEO steps down and the transition period, and Δ_C refers to the mean[median] difference in operating performance after the new CEO gets the combined title. ROA is calculated as the average[median] return on assets over the respective periods, while the industry adjusted ROA is the average[median] annual ROA net of industry mean, using two digit SIC codes to determine industry. Results for both the sample of successful successions and the ones where the new CEO is ousted before he can obtain the combined title are presented separately. Panel A presents the ROA, while Panel B presents the industry adjusted ROA. In Panel C, matched sample results are displayed using the Barber and Lyon (1997) method to match firms. The results for medians and the sign-rank test p-values on the differences are presented in brackets. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

Panel A: Return on Assets

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	3.42 [4.25]	3.09 [3.97]	5.02 [6.18]	-0.33 [-0.28]	-1.52 (0.1183) [0.1457]	1.93*** [2.21***]	2.97 (0.0000) [0.0000]
Ousted (N = 20)	2.76 [3.06]	1.82 [1.57]		-0.94 [-1.49*]	-1.49 (0.1201) [0.0814]		

Panel B: Industry Adjusted Return on Assets

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	1.15 [1.24]	0.92 [0.95]	2.18 [3.15]	-0.23 [-0.29]	-1.16 (0.1318) [0.1568]	1.26*** [2.20***]	2.85 (0.0000) [0.0000]
Ousted (N = 20)	0.89 [1.07]	0.27 [0.15]		-0.62 [-0.92*]	-1.41 (0.1127) [0.0731]		

(table continued)

Panel C: Barber and Lyon (1997) Matched Sample Return on Assets

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	1.10 [1.42]	0.94 [1.01]	2.31 [2.93]	-0.16 [-0.41]	-1.16 (0.1318) [0.1250]	1.37*** [1.92***]	2.91 (0.0000) [0.0000]
Ousted (N = 20)	0.91 [1.26]	0.34 [0.48]		-0.57 [-0.78]	-1.41 (0.1127) [0.1029]		

Furthermore, consistent with hypothesis 3 (H_3), for the 20 firms with unsuccessful probationary succession processes, where the new CEO end up being without being passed the baton, operating performance declines during the probationary period using all three measures. The results, however, are statistically insignificant looking at average ROA figures. This decline in operating performance, however, is significant using the median ROA and IAROA figures. The sign-rank test on the differences in operating performance shows that there is a significant decline in the median operating performance of firms during the probationary period, leading them to oust their incoming CEOs without passing them the baton.

Chapter 3 of my dissertation also states that these results would be expected both for accounting measures of operating performance and market value measures. Table 6.2 presents the mean abnormal stock returns for the firms using probationary succession processes for the same former CEO, probationary period and combined title periods.

The changes in the operating performance of firms using probationary succession processes display similar behavior using abnormal returns as well as accounting performance measures. Table 6.2 shows that the mean abnormal returns as well as the industry adjusted and matched sample mean abnormal returns for the firms in this sample

show no significant change during the probationary period. However, stock performance of the firms using probationary succession processes seem to significantly improve after the successful completion of the probationary period. The mean abnormal stock returns and the industry adjusted mean abnormal returns increase by 4.64% and 3.22%, respectively (with respective t-statistics of 5.99 and 3.79), both significant at the 1% level. The matched sample mean abnormal returns using the Barber and Lyon (1997) methodology increase by 2.63% after the completion of the probationary period, significant at 5% level (t-statistic = 2.05). The results are the same using the medians as well.

On the other hand, the stock performance of the 20 firms, which end up ousting their new CEOs without passing the baton decline significantly during the probationary period. This is consistent with H_3; firms using probationary succession processes will successfully oust their new CEOs if they "drop the baton." The mean abnormal returns for these 20 firms decline by 1.13% during the probationary period, from 1.26% during the last three years of the former chairman and CEO to only 0.13% during the probationary period. This decline is statistically significant at the 10% level, with a t-statistic of -1.70 and p-value of 0.0869. The industry adjusted and matched sample mean abnormal stock returns for firms with ousted new CEOs also show similar declines. The industry adjusted mean abnormal returns decline by 1.17% (t-statistic = -1.82) and the Barber and Lyon (1997) matched sample mean abnormal returns decline by 0.95% (t-statistic = -1.79), both significant at the 5% level. This decline is also present and sometimes more pronounced when median are used to run the same tests. The median results are presented in brackets.

Table 6.2
Stock Performance of Firms with Probationary Successions

Former CEO refers to the last three years of the former CEO's tenure before the succession took place. Probationary period refers to the transition period when the former CEO/current Chairman worked together with the new CEO, and the combined period refers to the first three years of the new CEO's tenure after he obtains the combined CEO and Chairman of the Board title. Δ_F presents the mean difference between the mean abnormal stock returns before the former CEO steps down and the transition period, and Δ_C refers to the mean difference in stock return performance after the new CEO gets the combined title. Mean [median] abnormal stock returns are the average abnormal stock returns during the respective periods, calculated as the mean [median] difference between the stock returns of the firm and the returns on the CRSP value-weighted index. Industry adjusted mean [median] abnormal returns are the average [median] abnormal returns for these periods net of the industry average calculated using two-digit SIC codes. Panel A presents the mean [median] abnormal returns, while Panel B presents the industry adjusted mean [median] abnormal returns. In Panel C, matched sample results are displayed using the Barber and Lyon (1997) method to match firms. The results for medians and the sign-rank test p-values on the differences are presented in brackets. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

Panel A: Abnormal Returns

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	2.25 % [2.68%]	1.37 % [1.42%]	6.01 % [6.93%]	-0.88 [-1.26]	-1.13 (0.1919) [0.1522]	4.64*** [5.51***]	5.99 (0.0000) [0.0000]
Ousted (N = 20)	1.26 % [1.78%]	0.13 % [0.19%]		-1.13* [-1.59**]	-1.70 (0.0869) [0.0481]		

Panel B: Industry Adjusted Abnormal Returns

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	1.36 % [1.30%]	0.12 % [0.17%]	3.34 % [4.08]	-1.24 [-1.13]	-1.34 (0.1843) [0.2057]	3.22*** [3.91***]	3.79 (0.0000) [0.0000]
Ousted (N = 20)	0.24 % [0.43%]	-0.93 % [-0.81%]		-1.17** [-1.24**]	-1.82 (0.0331) [0.0219]		

(table continued)

Panel C: Barber and Lyon (1997) Matched Sample Abnormal Returns

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value) [sign-rank p-value]	Δ_C	t-stat (p-value) [sign-rank p-value]
Successful (N = 183)	1.09% [1.15%]	0.32% [0.84%]	2.95% [3.49%]	-0.77 [-0.31]	-1.22 (0.1954) [0.2370]	2.63** [2.65***]	2.05 (0.0213) [0.0091]
Ousted (N = 20)	0.68% [0.79%]	-0.27% [-0.23%]		-0.95** [-1.02**]	-1.79 (0.0427) [0.0362]		

These results are also consistent with Brickley, Linck and Coles (1999), who find that post-retirement retention on CEOs own board or service on outside boards is dependent on the accounting and stock performance of the CEO's firm during his tenure. The increase in the operating performance of the firms after the end of the probationary period provide evidence to the existence of performance based incentives for departing CEOs as argued by Brickley, Linck and Coles (1999).

In addition to the accounting and stock performance of their firms, the reputation of a CEO also depends on the policies and business decisions he implements. Therefore, the former CEO would like to ensure that his policies are kept and followed. Simultaneously, the new CEO would have incentives to conform to the existent policies and keep the status quo in order to curry favor and complete the probationary period as quickly and easily as possible. Once the probationary period is complete, however, the incentives to conform cease to exist. Therefore, according to hypothesis 4 (H_4) presented in Chapter 3 of my dissertation, if managerial conformism exists in probationary succession processes, I would expect no change in the number of policy decisions taken during the probationary period. Yet, after the completion of the probationary period, I would expect a significant increase in the number of policy decisions. Table 6.3 presents

the number of policy decisions per year undertaken by the firm during the last three years of the former CEO, during the probationary period and the first three years of the new CEO.

The results presented in Table 6.3 show that there is a significant decline in both the average and the median number of policy decisions undertaken by firms with probationary succession processes during the probationary period. The mean (median) decline in the number of annual policy decisions during the probationary period is 1.38 (1), both statistically significant. This decrease in the number of annual policy decisions is also present in the firms with unsuccessful probationary successions. The average (median) decline in the number of annual policy decisions for firms with ousted new CEOs is 2.16 (2.5) decisions a year, both statistically significant at the 1% level. The decline in policy decisions for all probationary succession processes regardless of success or ousting, may be due to the large information transfer costs during the probationary period. It may take the new CEO a while to obtain all the critical strategic information about the company, and this information transfer period might be the cause for the significantly lower number of annual policy decisions during the probationary period.

The average (median) number of policy decisions also increases significantly at the end of the probationary period by 2.53 (2) decisions a year, both significant at the 1% level. This increase at the end of the probationary period is consistent with H_5. After the new CEO obtains the combined chairman/CEO title, his incentives to conform will be reduced, increasing the number of major policy decisions undertaken.

Table 6.3
Number of policy decisions by firms with probationary successions

The number of policy decisions for each firm have been determined by counting the results of a keyword search on Lexis-Nexis news and wire sources. All newsworthy events by the company with the exception of routine announcements of earnings, financial report filings, have been included as policy decisions. Former CEO refers to the last three years of the former CEO's tenure before the succession took place. Probationary period refers to the transition period when the former CEO/current Chairman worked together with the new CEO, and the combined period refers to the first three years of the new CEO's tenure after he obtains the combined CEO and Chairman of the Board title. Δ_F presents the mean difference between the number of policy decisions before the former CEO steps down and the transition period, and Δ_C refers to the difference in the number of policy decisions between the probationary period and after the new CEO gets the combined title. Results for both the sample of successful successions and the ones where the new CEO is ousted before he can obtain the combined title are presented separately. Panel A presents the mean number of policy decisions, while Panel B presents the median. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

Panel A: Mean Number of Policy Decisions

	Former CEO	Probationary Period	Combined Title	Δ_F	t-stat (p-value)	Δ_C	t-stat (p-value)
Successful (N = 183)	8.33	6.95	9.38	-1.38***	-7.04 (0.0000)	2.53***	8.26 (0.0000)
Ousted (N = 20)	8.27	6.11		-2.16***	-4.98 (0.0000)		

Panel B: Median Number of Policy Decisions

	Former CEO	Probationary Period	Combined Title	Δ_F	Sign-Rank Test p-value	Δ_C	Sign-Rank Test p-value
Successful (N = 183)	10	9	11	-1**	(0.0115)	2***	(0.0000)
Ousted (N = 20)	8.5	6		-2.5***	(0.0000)		

Table 6.4 presents a sample of the main policy decisions considered in this analysis. Major decisions were determined through a Lexis-Nexis search. All newsworthy events were recorded with the exceptions of routine earnings announcements, financial report filings or announcements made about the firm by other sources. Major policy announcements include managerial changes, downsizing, mergers and acquisitions, new production or financing lines and opportunities, new security issues, major asset sales and divestitures. One interesting aspect is the number of managerial, board member and board composition changes that coincide with succession periods. Of the 203 firms in the probationary succession sample, 187 (92%) have made changes to their board of directors around the succession period; 19 (9.35%) of these firms have actually changed the number of directors on their boards.

Table 6.4
Examples of Policy Decisions

This table presents some examples of policy decisions included in the analysis. These are not the entire policy changes, but they are a representative sample. The number of firms that have announced a policy decision like this have been presented in the second column.

Policy Decisions	Number of Firms
Management Changes	203
Changes in Board Members	187
Changes in Board Size	19
Downsizing	12
Mergers and Acquisitions	21
New Product Lines	37
Major Productive Investments (New plant, product facility expansions…etc)	28
New Credit Lines	53
New Debt Issues	71
Seasoned Equity Issues	4
Dividend Policy Changes (Increases, Decreases or Omissions of Dividends)	28
Chapter 11 Filings	3
Asset Sales	5
Joint Venture Agreements	12
Divestitures	17

6.2. Is managerial Conformism Detrimental for All Firms? Evidence from Rival Reactions

Managerial conformism is not necessarily costly or detrimental to a firm. Probationary succession processes are still very common in U.S. firms, suggesting that their benefits may outweigh potential costs for some firms. For some established, stable, well-performing corporations, managerial conformism may actually be an efficient means to transfer valuable information rather than being a source of loss of value. I will use the reaction of the firm's rivals to the announcement of a probationary succession process to determine whether managerial conformism is in fact detrimental to the firm or not. The rival firms used are the firms in the same four-digit SIC code. As stated in hypothesis 6 (H_6) in chapter 3, announcements of potentially costly managerial succession processes are expected to be accompanied by a positive stock price reaction from the firm's rivals. On the other hand, since managerial conformism exists in probationary succession processes, if this conformism is expected to be beneficial to the firm, the stock price reaction from the rivals is expected to be negative.

A sample of 526 rival firms has been created for the 183 firms in my sample. Table 6.5 presents the reactions of these rival firms to the probationary succession announcement. Rival firms of each succession firm in my sample have been grouped to form equally weighted rival portfolios. Then, the announcement reactions have been calculated using abnormal returns of the portfolio on the day of the probationary succession announcement and the cumulative abnormal returns on the [-1,0] two-day window around the announcement. The abnormal and cumulative abnormal returns have been estimated using a market model.

The average reaction of the rival firm portfolios to the announcement of a probationary succession process measured by the announcement day abnormal return is 0.0013, with a t-statistic of 1.21. The mean cumulative abnormal return earned by rival firm portfolios during the two-day announcement window is 0.0041, with a t-statistic of 1.30. The announcement returns on the rival firm portfolios using either measurement is not statistically significant. In other words, there is no market consensus on whether probationary succession processes are good or bad news.

Table 6.5
Rival Firm Announcement Returns

This table presents the reactions of rival firms to the announcement of probationary succession processes in the sample. The 526 rival firms in the same four-digit SIC code with the sample firms have been grouped into equally weighted rival firm portfolios for each succession-firm. Abnormal returns (AR) are the mean abnormal stock returns on the announcement day calculated based on a market model. Cumulative abnormal returns (CAR) are the two-day window [-1,0] announcement returns calculate again based on a market model. The twenty firms with incomplete probationary processes are excluded from the analysis. In parentheses are the t-statistics of the ARs and CARs. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

Overall Sample of Rival Firms Portfolios (N=183)		**Rival Firm Portfolios with Positive Reactions (N=110)**		**Rival Firm Portfolios with Negative Reactions (N = 73)**	
AR	0.0013	AR	0.0029*	AR	-0.0007
	(1.21)		(1.78)		(-1.55)
CAR	0.0041	CAR	0.0081*	CAR	-0.0042
	(1.30)		(1.90)		(-1.61)

However, based both on the announcement day abnormal returns and the two-day cumulative abnormal returns, 110 out of the 183 firms in my sample (60%) have rival firm portfolios that experience positive returns. The remaining 73 firms (40%) have rival firm portfolios with negative reactions. Moreover, the positive rival firm reactions are statistically significant at the 10% level of significance, while the negative reactions, measured by either method, are not statistically significant. These results indicate that,

consistent with the premise of this dissertation, managerial conformism is expected to be more costly than beneficial by the market.

Table 6.6
Rival Firm Reactions and Probationary Period Performance

This table presents the operating performance, stock performance and the number of policy decisions after the completion of the probationary period for firms with positive and negative rival firm portfolio reactions to the managerial succession announcement. Operating performance is measured by Return on Assets. Mean abnormal stock returns are the average abnormal stock returns during the respective periods, calculated as the mean difference between the stock returns of the firm and the returns on the CRSP value-weighted index. The number of policy decisions for each firm have been determined by counting the results of a keyword search on Lexis-Nexis news and wire sources. All newsworthy events by the company with the exception of routine announcements of earnings, financial report filings, have been included as policy decisions. T-statistics are presented in parentheses. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

Probationary Period Performance	Overall Sample (N=183)	Firms with Positive Rival Reactions (N=110)	Firms with Negative Rival Reactions (N=73)	Difference Test
Operating Performance (ROA)	3.09	2.47	4.02	-1.55** (2.01)
Stock Performance (Mean AR)	1.37	1.20	1.63	-0.43** (-1.97)
Number of Policy Decisions	6.95	6.60	7.47	-0.87 (1.65)

If the markets can efficiently determine whether the probationary succession process is costly or beneficial to the firm, then firms with beneficial probationary periods should significantly outperform those with costly succession periods during the probationary period. In other words, firms whose rival firm portfolios show positive announcement returns are expected to have significantly worse performance during the probationary period compared to those firms with negative rival firm portfolio announcement returns. Table 6.6 compares the accounting operating performance, stock performance and number of policy decisions during the probationary period for firms with positive and negative rival firm portfolio reactions. The results are consistent with my expectation that firms with costly managerial conformism also significantly

underperform during the probationary period compared to the firms with beneficial managerial conformism.

The existence of managerial conformism is documented above by the change in operating performance, stock performance and number of policy decisions of a firm at the end of the probationary period. Therefore, I compare these variables for firms in my sample whose rivals show positive reactions and those whose rivals show negative reactions. Table 6.7 presents these results.

Table 6.7
Rival firm reactions and managerial conformism

This table presents the changes in operating performance, stock performance and the number of policy decisions after the completion of the probationary period for firms with positive and negative rival reactions to the managerial succession announcement. Δ_C refers to the mean difference in these variables after the new CEO gets the combined title. Operating performance is measured by Return on Assets. Mean abnormal stock returns are the average abnormal stock returns during the respective periods, calculated as the mean difference between the stock returns of the firm and the returns on the CRSP value-weighted index. The number of policy decisions for each firm have been determined by counting the results of a keyword search on Lexis-Nexis news and wire sources. All newsworthy events by the company with the exception of routine announcements of earnings, financial report filings, have been included as policy decisions. T-statistics are presented in parentheses. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

ΔC	**Overall Sample (N=183)**	**Firms with Positive Rival Reactions (N=110)**	**Firms with Negative Rival Reactions (N=73)**	**Difference Test**
Operating Performance (ROA)	1.93***	2.18***	1.55*	0.63*
	(2.97)	(3.14)	(1.73)	(1.78)
Stock Performance (Mean AR)	4.64***	5.92***	2.71*	3.21*
	(5.99)	(6.01)	(1.70)	(1.70)
Number of Policy Decisions	2.53***	3.49***	1.08*	2.41**
	(8.26)	(8.29)	(1.81)	(2.01)

Firms have been grouped into those with positive reactions from their rival firm portfolios and those with negative rival reactions based on the sign of the mean rival firm portfolio reaction for each firm. The results in Table 6.7 show that the increase in operating performance, stock performance and the number of policy decisions at the

completion of the probationary period is significantly higher for firms with positive rival reactions. This result is consistent with my expectation that if the costs of managerial conformism are high, then the rivals of the firm should benefit from the decision of managerial succession. In other words, the market anticipates the incentive problems between the departing and the incoming CEOs in a probationary succession process and the stock prices of the rival firms reflect this anticipation at the announcement of the managerial succession plan. These findings imply that probationary succession processes should only be used by firms that can shoulder these agency costs.

The next question that follows this is: Which firms should use probationary succession processes? Since the conflicts of interest that arise in these managerial succession schemes are detrimental only to certain firms, I try to see whether there is a difference between the characteristics of the firms with positive rival reactions to probationary succession and those with negative reactions. Table 6.8 compares the descriptive statistics of the two sub-samples to see whether there are any differences.

Consistent with Parrino (1997), Huson, Malatesta and Parrino (2001) and Naveen (2003), firms that receive negative reactions from their rivals, in other words have potentially beneficial probationary succession processes, are significantly larger in terms of their median. The mean size of the firms is not statistically different, but this may be due to the large variation in the size of the firms in my sample.

The results in Table 6.8 also show that firms with negative rival reactions have significantly larger percentage of institutional ownership, board stock ownership and a higher percentage of outside members on the board. This indicates that better outside and board monitoring in the firm serves as a signal to the market that less conflicts of interest

are likely to arise during the probationary period. In other firms, the costs of probationary succession processes are not detrimental in firms with efficient monitoring mechanisms.

Table 6.8
Descriptives of the firms with positive and negative rival reactions

CEO ages, prior time spent in the firm and the departing CEO tenure as CEO are all measured in terms of years. Departing CEO and chairman share ownership and institutional ownership measure the percentage of the firm's stock owned by the incumbent CEO and by institutional investors, respectively. Board Stock ownership measures the percentage of the firm's shares owned by Board members except the departing and/or incoming CEO and the Chairman of the Board. Probationary period is the number of years it takes for new CEO to be granted the combined CEO/Chairman of the Board title, during which the old and the new CEO work together. Board size is the number of directors that serve on the board of the firm. The percentage of outside board members measures the proportion of directors on the Board of the firm that are not former employees of the firm and have no business relationships with the firm. Sales and assets of the firms are also presented in millions of dollars. T-statistics for the difference in means test and Wilcoxon z-statistics for the difference in medians tests are provided. *, ** and *** represents significance at the 10%, 5% and 1% levels, respectively.

	Firms with Positive Rival Reactions (N=110)		Firms with Negative Rival Reactions (N=73)		Difference in Means Test	Difference in Medians Test
Variable	**Mean**	**Median**	**Mean**	**Median**	**t-stat**	**z-stat**
Departing CEO and Chairman Age	63.12	64	59.93	62	1.67	1.59
Departing CEO and Chairman Tenure as Chairman	8.94	8	7.26	6.5	1.70*	1.82*
Departing CEO and Chairman Tenure as CEO	10.15	9	8.30	8	1.76*	1.80*
Departing CEO and Chairman Prior Time with the Firm	22.57	19	20.39	15	1.49	1.61
Departing CEO and Chairman Share Ownership (%)	5.72	1.42	6.01	1.40	-1.09	0.62
Incoming CEO Age	51.39	50	48.23	50	1.43	1.04
Incoming CEO Prior Time with the Firm	8.27	4	10.05	6	-1.91*	-1.76*
Incoming CEO Prior Time as a director on the board	1.87	2	2.16	3	-2.01**	-1.64
Incoming CEO Share Ownership (%)	1.21	<1	1.96	<1	-1.23	-0.59
Length of the Probationary Period	3.53	3	2.20	2	1.89*	1.70*
Board Size	9.27	9	8.11	9	1.16	0.94
Outside Board Members (%)	27.19	30	41.38	40	-2.05**	-1.97**
Institutional Ownership (%)	31.04	35	37.21	38	-3.10***	-1.89*
Board Stock Ownership (%)	5.71	2	6.18	3	-1.74*	-1.80*
Market Capitalization ($millions)	1472.1	124.41	1645.94	205.36	1.09	-2.34***

The results in this chapter show that managerial conformism does exist in probationary succession processes. Consistent with expectations, there are no changes in operating performance, stock performance or the number of policy decisions undertaken during the probationary period. Yet, all of these measures improve significantly at the conclusion of the test period. Probationary processes also serve to successfully oust non-performing incoming CEOs before they can obtain the combined title.

Managerial conformism is not exactly detrimental for all firms though. My results using the reaction of rival firms to the managerial succession announcements show that larger firms with better means of external control can beneficially use the relay-race-type succession process.

CHAPTER 7
FACTORS THAT INFLUENCE THE LEVEL OF MANAGERIAL CONFORMISM: REGRESSION RESULTS

This chapter provides results from regression analysis to determine the factors and the levels to which these factors influence managerial conformism. Several different regression analyses have been used in this section to distinguish the determinants of managerial conformism.

Table 7.1 presents the results of logit regressions that directly measure the probability of managerial conformism in a firm. The dependent variable is set equal to one if there is an increase in the number of policy decisions after the probationary period is over and there is also an increase in the operating performance of the firm measured by both the ROA and industry adjusted ROA.[17] Independent variables measuring managerial entrenchment, effectiveness of board and outside monitoring, the departing CEO's stock ownership in the firm, post-retirement employment possibilities and incoming CEO's characteristics are included in these regressions. Additionally, control variables that measure firm characteristics like firm size, age, market-to-book ratio and the number of business segments are included.

If the departing CEO is more entrenched in the company, conflicts of interest between the former and new CEOs will be greater. Following hypotheses H_9 through H_{12} in Chapter 3, the following entrenchment variables are included in the regression:

- The tenure of the departing CEO as chairman or as CEO
- The time the departing CEO has spent as an employee of the firm

[17] Same analysis has been conducted with a dummy variable that equals one if the matched sample ROA increases after the probationary period is over. The results are qualitatively the same, so only one of the regressions have been presented.

- A dummy variable that takes the value of one if the departing CEO is the founder of the firm or a member of the founding family
- A dummy variable that takes the value of one if the departing CEO is the founder or a member of the founding family, but will be succeeded by an individual outside the founding family

The longer time the departing CEO has spent as an employee of the firm or in the CEO position, the more the former CEO is expected to get entrenched to the firm. More entrenched CEOs are expected to have greater presence on the board as well as the general corporate culture of the firm, increasing the probability of managerial conformism.

On the other hand, effective board monitoring of manager actions as well as outside monitoring of the firm is expected to reduce the agency conflicts between the departing and the incoming CEOs, and thus reduce the probability of managerial conformism. The percentage stock ownership by institutional investors, stock ownership by board members who are not chairmen or CEOs and the percentage of outsiders that sit on the board are used to measure the effectiveness of outside and board monitoring on the firm. I expect these variables to reduce the probability of managerial conformism. On the other hand, board size is included as a measure of board efficiency, and I expect larger boards to be less effective monitors.

If the departing CEO is retained on the board of directors of his own firm, then the probability of managerial conformism should increase, since the influence of the former CEO will still be apparent on the board even after the conclusion of the probationary period. However, if the incoming CEO has been employed with the firm for

Table 7.1
Determinants of the Probability of Managerial Conformism

The results of a logit regression predicting the probability of managerial conformism are presented. The dependent variable has been set equal to one if there is an increase in the number of policy decisions after the transition period is over and there is an improvement in the operating performance of the firm measured by both ROA and industry adjusted ROA, after the transition period is over. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Departing CEO tenure measures the number of years the departing CEO has been holding the office of CEO prior to stepping down. Founder is a dummy variable that takes the value of one if the former CEO is the founder of the company or a member of the founding family. Founder replaced by non-founder is a dummy variable that takes the value of one if a member of the founding family is replaced as CEO by a successor who is not from the founding family. Institutional ownership, departing CEO ownership and Board of directors ownership represent the percentage of stock ownership by institutional investors, by the departing CEO and by the members of the board that are neither Chairman or CEO. Board size measures the number of directors sitting on a firm's board. Finally the percentage of outside board membership measures the ratio of the board members that are not former employees of the firm or have business relationships with the firm to the entire size of the Board of Directors. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Control Variables	Intercept	0.92	0.53	0.48	0.82	0.99	0.97	0.54	0.95	0.55
		(0.84)	(0.58)	(0.52)	(1.01)	(1.11)	(1.10)	(0.88)	(1.04)	(0.71)
	Log Size	-0.86**	-0.54**	-0.56**	-0.69**	-0.53**	-0.49**	-0.45**	-0.59**	-0.79**
		(-2.28)	(-2.25)	(-2.16)	(-2.29)	(-2.12)	(-2.18)	(-2.08)	(-2.04)	(-2.23)
	Firm Age	-0.04*	-0.04*	-0.05*	-0.04*	-0.06*	-0.05*	-0.03*	-0.01	-0.08**
		(-1.72)	(-1.74)	(-1.76)	(-1.79)	(-1.76)	(-1.88)	(-1.69)	(-1.58)	(-1.99)
	Market-to-Book	0.003	0.005	0.003	0.004	0.003	0.007	0.005	0.004	0.001
		(0.79)	(0.57)	(0.46)	(0.86)	(0.72)	(1.06)	(1.05)	(0.87)	(0.69)
	Number of Business Segments	0.002	0.004	0.007	0.003	0.002	0.005	0.008	0.006	0.004
		(1.03)	(1.07)	(1.10)	(1.07)	(1.04)	(1.06)	(1.12)	(1.11)	(1.06)
	Departing CEO Ownership	-0.0042								
		(-1.29)								
Entrenchment Variables	Departing CEO Tenure		0.103***							
			(2.79)							
	Departing CEO Time Employed in the Company			0.093**						
				(2.01)						
	Founder?				0.95***					
					(4.03)					
	Founder Replaced by Non-founder					0.87***				
						(3.48)				
Monitoring Variables	Institutional Ownership						-0.008			
							(-1.16)			
	Board Ownership							-0.006*		
								(-1.92)		
	Board Size								-0.002	
									(-1.05)	
	Outside Board Members									-0.01
										(-1.15)
	R^2	0.22	0.31	0.29	0.30	0.31	0.27	0.30	0.29	0.33
	N	183	183	183	183	183	183	183	183	183

Table 7.1 (continued)

The results of a logit regression predicting the probability of managerial conformism are presented. The dependent variable has been set equal to one if there is an increase in the number of policy decisions after the transition period is over and there is an improvement in the operating performance of the firm measured by both ROA and industry adjusted ROA, after the transition period is over. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Retained on own board, chairman emeritus and served on other boards are dummy variables that take the value of one if the departing CEO remain on his own board as a director, serves as chairman emeritus or serves as a director on other companies' boards, respectively. Incoming CEO's time with the company measures the number of years the incoming CEO has been employed by the company. Incoming CEO stock ownership measures the percentage stock ownership of the incoming CEO, while the dummy variable outsider takes the value of one if the incoming CEO is an outsider. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

		(10)	(11)	(12)	(13)	(14)	(15)
Control Variables	Intercept	0.43	0.97	0.55	0.37	0.67	0.71
		(0.51)	(1.09)	(0.70)	(0.41)	(0.82)	(0.88)
	Log Size	-0.85**	-0.56**	-0.74**	-0.59**	-0.69**	-0.57**
		(-2.29)	(-2.14)	(-2.21)	(-2.15)	(-2.18)	(-2.14)
	Firm Age	-0.02*	-0.04*	-0.05*	-0.04*	-0.06*	-0.05*
		(-1.72)	(-1.74)	(-1.76)	(-1.76)	(-1.76)	(-1.74)
	Market-to-Book	0.003	0.002	0.003	0.005	0.007	0.004
		(0.76)	(0.68)	(0.74)	(0.99)	(1.02)	(0.89)
	Number of Business Segments	0.006	0.004	0.007	0.002	0.005	0.009
		(1.05)	(1.02)	(1.11)	(1.01)	(1.06)	(1.15)
Post-Retirement Employment	Retained on own board?	0.85***					
		(3.42)					
	Chairman Emeritus?		0.49**				
			(2.15)				
	Serves on other boards?			-0.21			
				(-1.54)			
Incoming CEO Characteristics	Incoming CEO time employed in the company				-0.24*		
					(-1.78)		
	Incoming CEO stock ownership					-0.008**	
						(-2.09)	
	Outsider?						-0.96***
							(-2.54)
	R^2	0.20	0.29	0.24	0.27	0.29	0.25
	N	183	183	183	183	183	183

a long time and has significant stock ownership in the firm, then his incentives to conform would be lowered, decreasing the probability of managerial conformism.

The results presented in Table 7.1 show that consistent with H_{21} larger and older firms have a lower probability of managerial conformism. In all sixteen regression equations, both firm size and age have consistently negative and significant effects on the probability of managerial conformism. On the other hand, market-to-book ratios and the number of business segments have no significant effects on the probability of managerial conformism.

All four of the entrenchment variables significantly increase the probability of managerial conformism, while only the percentage of share ownership by non-CEO and non-chairman board members, out of the monitoring variables, seems to have a reducing effect on the probability of managerial conformism. The other variables measuring the monitoring effectiveness of the board and outside factors, namely board size, percentage of outsiders on the board and the percentage of institutional ownership, have negative coefficients as expected, yet none of these factors seem to have statistically significant effects on the probability of managerial conformism.

The incentive conflicts between the departing and incoming CEOs would be reduced in the Jensen and Meckling (1976) sense with increases in the share ownership of the departing CEO. Since these shares owned by the departing CEO would align his interests with those of the shareholders and thus the new CEO, agency conflicts should be reduced, reducing the probability of managerial conformism. The coefficient for the departing CEO ownership variable in Table 7.1 is accordingly negative, yet insignificant;

implying that departing CEO's stock ownership does not provide him with enough incentives to forego advocating conformism.

The post-retirement career opportunities of the departing CEO are what create the conflicts of interest in the first place. Regressions (10) and (11) show that departing CEOs who are retained on their own boards as directors or chairman emeriti increase the probability of managerial conformism. Both variables have statistically significant positive coefficients. However, the coefficient for the "serve on other boards?" variable is negative though not statistically significant. This result inconsistent with H_{20} may mean that the incentives provided by efficient labor markets work to reduce managerial conformism problems.

Aligning the incentives of the incoming CEO with those of the shareholders seems to help reduce the incentives of the newcomer to conform in order to curry favor and reduce the length of the probationary period. The longer the new CEO has worked in the company before becoming CEO and the higher the percentage of his stock ownership, the lower is the probability of managerial conformism. Both these results are statistically significant. In other words, incoming CEO's incentives to conform are reduced, the more familiar he is with the corporate culture of the company. On the other end of the spectrum, if the new CEO is an outsider, then the probability of managerial conformism is significantly lower than if the incoming CEO is an insider.

The length of the probationary period can serve as a proxy for the severity of the agency costs between the incumbent/departing and the new CEOs in probationary succession processes, since the more the departing CEO tries to secure the continuation of his policies, the longer it would take for the new CEO to pass the test, and be awarded

the combined title of CEO and chairman of the board. Moreover, the more conflicts of interest arise between the incumbent and the new CEO, the harder it would be and the longer it would take for the new CEO to successfully complete the probationary period. Table 7.2 presents regression results using the length of the probationary period as the dependent variable and the same determinants of managerial conformism as the independent variables.

Similar to the results in Table 7.1, results presented in this table also show that firm size and age reduce the problems associated with managerial conformism. The probationary period is significantly shorter in larger and older firms. All measures of managerial entrenchment have significantly positive coefficients. The more entrenched the departing CEO is, the longer the probation process takes. This is expected since more entrenched CEOs are will have more incentives to ensure that their successors conform. At the same time, the more entrenched departing CEOs will have more power over the other members of the board, making the probationary period longer and harder for the successor.

On the other hand, all independent variables used to measure board and outside monitoring on the firm, except for board size, significantly reduce the length of the probationary period. Firms with boards with a higher percentage of outside members and firms where the stock ownership of the board members other than the CEO and the chairman are high have significantly shorter probationary periods. Increased institutional ownership significantly reduces the probation period as well (t-statistic = -2.07). Only board size seems to have an insignificant effect (t-statistic = -1.57).

Table 7.2
Determinants of the Length of the Probationary Period

The dependent variable in the regression models is the length of the probationary period, in years, when the new CEO and the departing CEO/current Chairman work together. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Departing CEO tenure measures the number of years the departing CEO has been holding the office of CEO prior to stepping down. Founder is a dummy variable that takes the value of one if the former CEO is the founder of the company or a member of the founding family. Founder replaced by non-founder is a dummy variable that takes the value of one if a member of the founding family is replaced as CEO by a successor who is not from the founding family. Institutional ownership, departing CEO ownership and Board of directors ownership represent the percentage of stock ownership by institutional investors, by the departing CEO and by the members of the board that are neither Chairman or CEO. Board size measures the number of directors sitting on a firm's board. Finally the percentage of outside board membership measures the ratio of the board members that are not former employees of the firm or have business relationships with the firm to the entire size of the Board of Directors. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Control Variables	Intercept	1.29	1.23	1.31	1.33	1.12	1.46	1.11	1.06	1.15
		(0.68)	(0.56)	(0.72)	(0.74)	(0.45)	(0.80)	(0.77)	(0.53)	(0.47)
	Log Size	-2.04**	-1.99**	-2.07**	-2.10**	-2.13**	-2.18**	-2.19**	-2.28***	-2.07***
		(-2.18)	(-1.87)	(-2.04)	(-2.12)	(-2.09)	(-2.10)	(-2.07)	(-2.40)	(-2.00)
	Firm Age	-1.01*	-1.12**	-1.05**	-1.00*	-1.04*	-1.09*	-1.03*	-0.98*	-1.08*
		(-1.95)	(-2.07)	(-2.01)	(-1.71)	(-1.73)	(-1.78)	(-1.83)	(-1.72)	(-1.89)
	Market-to-Book	-0.034	0.020	0.016	-0.024	-0.048	0.002	-0.001	0.029	0.027
		(-1.15)	(0.71)	(0.53)	(-0.85)	(-1.19)	(0.32)	(-0.59)	(0.91)	(1.03)
	Number of Business Segments	0.56**	0.68**	0.42*	0.32*	0.74**	0.81**	0.29	0.47*	0.93**
		(1.92)	(1.94)	(1.69)	(1.69)	(1.87)	(1.95)	(1.68)	(1.71)	(1.97)
	Departing CEO Ownership	-0.17								
		(-1.42)								
Entrenchment Variables	Departing CEO Tenure		0.63**							
			(2.27)							
	Departing CEO Time Employed in the Company			0.78***						
				(2.34)						
	Founder?				2.09***					
					(3.25)					
	Founder Replaced by Non-founder					2.03***				
						(3.07)				
Monitoring Variables	Institutional Ownership						-0.11**			
							(-2.07)			
	Board Ownership							-0.66***		
								(-2.64)		
	Board Size								-0.25	
									(-1.57)	
	Outside Board Members									-0.79**
										(-2.04)
	R^2	0.03	0.05	0.04	0.07	0.05	0.04	0.06	0.05	0.08
	N	183	183	183	183	183	183	183	183	183

Table 7.2 (continued)

The dependent variable in the regression models is the length of the probationary period, in years, when the new CEO and the departing CEO/current Chairman work together. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Retained on own board, chairman emeritus and served on other boards are dummy variables that take the value of one if the departing CEO remain on his own board as a director, serves as chairman emeritus or serves as a director on other companies' boards, respectively. Incoming CEO's time with the company measures the number of years the incoming CEO has been employed by the company. Incoming CEO stock ownership measures the percentage stock ownership of the incoming CEO, while the dummy variable outsider takes the value of one if the incoming CEO is an outsider. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

		(10)	(11)	(12)	(13)	(14)	(15)
Control Variables	Intercept	1.09	1.11	1.31	1.42	1.29	1.38
		(0.54)	(0.77)	(0.72)	(0.78)	(0.68)	(0.80)
	Log Size	-2.23**	-2.04**	-1.99**	-2.15**	-2.07**	-2.19**
		(-2.24)	(-2.07)	(-1.87)	(-2.09)	(-2.04)	(-2.07)
	Firm Age	-1.03*	-1.01*	-1.09*	-1.08*	-1.05**	-1.07*
		(-1.83)	(-1.95)	(-1.78)	(-1.81)	(-2.01)	(-1.92)
	Market-to-Book	0.003	-0.001	0.002	-0.034	-0.013	0.005
		(0.34)	(-0.59)	(0.32)	(-1.15)	(-0.99)	(0.47)
	Number of Business Segments	0.90*	0.81**	0.74**	0.56**	0.42*	0.32*
		(1.87)	(1.95)	(1.87)	(1.92)	(1.71)	(1.70)
Post-Retirement Employment	Retained on own board?	1.89					
		(1.45)					
	Chairman Emeritus?		1.54				
			(1.28)				
	Serves on other boards?			2.01***			
				(3.15)			
Incoming CEO Characteristics	Incoming CEO time employed in the company				-1.42**		
					(-2.06)		
	Incoming CEO stock ownership					-0.68***	
						(-3.71)	
	Outsider?						-1.84*
							(-1.93)
	R^2	0.05	0.02	0.04	0.03	0.05	0.04
	N	183	183	183	183	183	183

Whether the departing CEO is retained on his own firm's board as a director at the end of the probationary period or not has no significant effect on the length of the probationary period. The coefficients for the dummy variables that measure whether the departing CEO remain on his own board as a director or as chairman emeritus are both positive but statistically not significant (t-statistics equal 1.45 and 1.28, respectively). Yet, the probationary period for the successors of those departing CEOs, who go on to serve on other firms' boards, is significantly longer (t-statistic = 3.15).

The characteristics of the successor are again important in determining the level of managerial conformism in the firm. The length of the probationary period is significantly shorter in firms where the incoming CEO has been employed in the company for longer periods of time and owns more stock. Furthermore, if the successor is an outsider, the probationary period is significantly reduced (t-statistic = 1.93).

Similar again to the results in Table 7.1, the stock ownership of the departing CEO does not have any significant effects on the length of the probationary period, implying that the basic solution of aligning shareholder and departing manager's incentives is not enough to solve this agency problem.

The tests presented in tables 7.1 and 7.2 have also been redone by restricting the sample to firms with probationary periods between 6 months and 6 years, leaving out 4 outliers. However, the results are qualitatively the same.

Due to the high correlations between the proxies used in the regression specifications, most of the power of the tests disappears when all variables are used in the regression. To remedy this problem, I carry out a principal components analysis with the 15 proxy variables used in these regressions to measure managerial entrenchment,

monitoring effectiveness of the board, departing CEO's post-retirement employment opportunities and the incoming CEO's characteristics. Five components result with eigenvalues greater than one. The three components with eigenvalues greater than one that have high loadings on entrenchment variables, post-retirement employment dummies and incoming CEO variables have been named entrenchment component, post-retirement component and incoming CEO component, respectively. Two of the components with eigenvalues greater than one have high loadings on monitoring efficiency variables. One of them has the highest loading on institutional ownership variable, while the other one loads on the stock ownership of board members. These two components have been called monitoring component (institutional ownership) and monitoring component (board ownership), respectively. The logit and OLS regressions presented in tables 7.1 and 7.2 have been redone using these components as independent variables in addition to the control variables. The results are presented in tables 7.3 and 7.4.

As presented in Table 7.3, using the components derived from the principal components analysis does not change the results. Larger and older firms, since they are easier to monitor and compare, have significantly lower probability of managerial conformism. While the entrenchment of the departing CEO significantly increases the probability of managerial conformism, the incoming CEOs tenure and stock ownership reduce the probability of managerial conformism. More effective monitoring by institutional investors and aligning the incentives of the directors with those of the shareholders work to reduce the probability of managerial conformism. Also, departing CEOs with more post-retirement opportunities seem to have a higher likelihood to engage in managerial conformism. Departing CEO's stock ownership does not seem to be

effective in aligning the interests of the departing CEO with those of the shareholders and reducing managerial conformism.

Table 7.3
Determinants of the Probability of Managerial Conformism
(Using the Principal Components Analysis Results)

The results of a logit regression predicting the probability of managerial conformism are presented. The dependent variable has been set equal to one if there is an increase in the number of policy decisions after the transition period is over and there is an improvement in the operating performance of the firm measured by both ROA and industry adjusted ROA, after the transition period is over. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Managerial entrenchment, monitoring, post-retirement career and incoming CEO components are the five components with eigenvalues greater than one in the principal components analysis. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Intercept	0.31	0.14	0.13	0.24	0.26	0.03
	(1.49)	(1.35)	(1.29)	(1.33)	(1.41)	(1.25)
Log Size	-0.73*	-0.58*	-0.61*	-0.64*	-0.52*	-0.46*
	(-1.75)	(-1.72)	(-1.70)	(-1.81)	(-1.77)	(-1.74)
Firm Age	-0.004*	-0.003*	-0.002*	-0.006*	-0.005*	-0.004*
	(-1.89)	(-1.84)	(-1.81)	(-1.92)	(-1.90)	(-1.91)
Market-to-Book	0.001	-0.004	-0.008	0.002	-0.003	0.004
	(0.27)	(-0.41)	(-0.74)	(0.19)	(-0.34)	(0.46)
Number of Business Segments	0.001	0.002	0.007	0.003	0.002	0.005
	(1.49)	(1.51)	(1.63)	(1.56)	(1.50)	(1.59)
Departing CEO Stock Ownership	-0.17	-0.14	-0.21	-0.16	-0.20	-0.19
	(-1.54)	(-1.48)	(-1.62)	(-1.51)	(-1.58)	(-1.58)
Managerial Entrenchment	0.92***					0.11*
Component	(2.34)					(1.78)
Monitoring Component		-0.51***				-0.16*
(Institutional Ownership)		(-3.22)				(-1.90)
Monitoring Component			-0.24**			-0.18*
(Board Ownership)			(-2.05)			(-1.84)
Post-Retirement				0.05**		0.03*
Career Component				(1.99)		(1.70)
Incoming CEO Component					-0.19***	-0.04*
					(-2.50)	(-1.89)
R^2	0.32	0.39	0.37	0.30	0.31	0.47
N	183	183	183	183	183	183

Table 7.4 repeats the analysis in Table 7.2 using the principal components instead of the actual proxies as independent variables. The results are similar to those is Table 7.2 and 7.3. The only interesting observation in Table 7.4 is that the component

measuring the post-retirement career opportunities of the departing CEO loses its significance when paired with other explanatory variables.

Table 7.4
Determinants of the Length of the Probationary Period
(Using the Principal Components Analysis Results)

The dependent variable in the regression models is the length of the probationary period, in years, when the new CEO and the departing CEO/current Chairman work together. Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Managerial entrenchment, monitoring, post-retirement career and incoming CEO components are the five components with eigenvalues greater than one in the principal components analysis. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Intercept	1.14	1.16	1.35	1.26	1.20	1.08
	(0.93)	(0.95)	(1.12)	(1.07)	(1.05)	(0.79)
Log Size	-1.72*	-1.82**	-1.70*	-1.68*	-1.71*	-1.59*
	(-1.94)	(-1.99)	(-1.90)	(-1.89)	(-1.90)	(-1.77)
Firm Age	-0.03*	-0.04*	-0.02*	-0.02*	-0.05*	-0.03*
	(-1.86)	(-1.90)	(-1.75)	(-1.75)	(-1.90)	(-1.88)
Market-to-Book	0.002	0.005	0.004	0.005	0.003	0.004
	(1.42)	(1.56)	(1.50)	(1.54)	(1.52)	(1.52)
Number of Business Segments	1.07	1.03	1.04	1.06	1.02	1.02
	(1.53)	(1.43)	(1.46)	(1.50)	(1.40)	(1.41)
Departing CEO Stock Ownership	-1.10	-1.09	-1.05	-1.06	-1.12	-1.02
	(-0.98)	(-0.99)	(-0.98)	(-0.97)	(-0.99)	(-0.91)
Managerial Entrenchment	2.07**					-1.58*
Component	(1.97)					(-1.89)
Monitoring Component		-0.78***				-0.74**
(Institutional Ownership)		(-3.01)				(-2.06)
Monitoring Component			-2.13***			-1.88**
(Board Ownership)			(-2.45)			(-1.97)
Post-Retirement				1.58*		1.40
Career Component				(1.70)		(1.63)
Incoming CEO Component					-1.08**	-1.01**
					(-2.00)	(-1.99)
R^2	0.05	0.04	0.04	0.05	0.05	0.09
N	183	183	183	183	183	183

The more serious the agency problem between the departing and the incoming CEO during the probationary period, the higher should the increase be in the operating performance of the firm at the end of the probationary period. As managerial conformism increases, the effects of the successful completion of the probationary period

should be more pronounced. Therefore, I run similar regressions models on the increase in operating performance, measured both by ROA and abnormal stock returns, and the increase in the number of policy decisions. Table 7.5 shows the results for the regression models using the change in operating performance, measured by the change in ROA[18] at the end of the probationary period, as the dependent variable and the entrenchment, monitoring, post-retirement and incoming CEO components.

Results are similar to those presented in previous tables. Managerial conformism is significantly higher in smaller and younger firms. The level of diversification in the firm or the firm's growth potential does not seem to have significant effects on the level of managerial conformism. The stock ownership of the departing CEO fails to reduce the level of managerial conformism again. Consistent with expectations, the regression coefficients of the departing CEO ownership variable are negative in all six regression models; yet, the effect is not statistically significant. Again similar to the previous tables, entrenchment of the departing CEO inflates the managerial conformism problem, while effective board and outside controlling reduces it. The component measuring the post-retirement career opportunities of the departing CEO has a significantly positive coefficient, consistent with the hypotheses in chapter 3.

Table 7.6 repeats the same tests for the level of managerial conformism using stock performance as the dependent variable. The results are again similar to those in the previous tables. Older and larger firms experience significantly lower levels of managerial conformism, while the level of diversification or the growth potential of the

[18] Similar regressions have been run using the increases in industry adjusted ROA and Barber and Lyon (1997) matched sample ROA, but the results are qualitatively the same. Therefore, in order to be consistent with literature ROA results have been presented.

firm, measured by market-to-book ratio have no significant effects on the level of managerial conformism.

Table 7.5
Determinants of the Change in Operating Performance
(Using the Principal Components Analysis Results)

The dependent variable in the regression models is the change in the operating performance (change in ROA) of the firm upon the conclusion of the probationary period when the new CEO takes on the combined CEO and Chairman of the Board title (i.e. Δ_C) Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Managerial entrenchment, monitoring, post-retirement career and incoming CEO components are the five components with eigenvalues greater than one in the principal components analysis. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Intercept	1.06	1.18	1.26	1.01	1.36	1.13
	(1.21)	(1.36)	(1.41)	(1.24)	(1.51)	(1.29)
Log Size	-1.61*	-1.58*	-1.72*	-1.64*	-1.69*	-1.52*
	(-1.74)	(-1.77)	(-1.80)	(-1.75)	(-1.78)	(-1.72)
Firm Age	-0.04*	-0.03*	-0.05*	-0.02*	-0.04*	-0.02*
	(-1.89)	(-1.84)	(-1.89)	(-1.81)	(-1.90)	(-1.80)
Market-to-Book	-0.003	0.005	-0.001	-0.008	-0.004	0.003
	(-0.34)	(0.42)	(-0.20)	(-0.74)	(-0.41)	(0.32)
Number of Business Segments	0.007	0.003	0.002	0.006	0.003	0002
	(1.63)	(1.54)	(1.50)	(1.60)	(1.53)	(1.51)
Departing CEO Stock Ownership	-1.02	-0.99	-1.05	-1.03	-1.04	-0.92
	(-1.40)	(-1.34)	(-1.42)	(-1.39)	(-1.39)	(-1.36)
Managerial Entrenchment	2.12***					2.03**
Component	(2.77)					(2.01)
Monitoring Component		-1.31**				-1.29*
(Institutional Ownership)		(-1.99)				(-1.90)
Monitoring Component			-1.25*			-1.20*
(Board Ownership)			(-1.84)			(-1.83)
Post-Retirement				1.94**		1.57*
Career Component				(2.07)		(1.89)
Incoming CEO Component					-1.53**	-1.34*
					(-2.18)	(-1.87)
R^2	0.07	0.06	0.03	0.05	0.05	0.08
N	183	183	183	183	183	183

The five principal components act according to expectations in table 7.6 as well. However, firm age ceases to be a significant determinant of managerial conformism, when the change stock performance at the end of the probationary period is used as the dependent variable.

Table 7.6
Determinants of the Change in Stock Performance
(Using the Principal Components Analysis Results)

The dependent variable in the regression models is the change in the abnormal stock returns of the firm upon the conclusion of the probationary period when the new CEO takes on the combined CEO and Chairman of the Board title (i.e. Δ_C). Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Managerial entrenchment, monitoring, post-retirement career and incoming CEO components are the five components with eigenvalues greater than one in the principal components analysis. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Intercept	0.36	0.71	0.49*	0.34	0.67*	0.45
	(1.68)	(1.66)	(1.72)	(1.67)	(1.89)	(1.64)
Log Size	-0.89*	-0.65*	-0.62*	-0.73*	-0.60*	-0.75*
	(-1.94)	(-1.76)	(-1.71)	(-1.89)	(-1.71)	(-1.82)
Firm Age	-0.06	-0.03	-0.03	-0.05	-0.03	-0.05
	(-1.63)	(-1.44)	(-1.44)	(-1.62)	(-1.49)	(-1.62)
Market-to-Book	-0.008	0.005	0.004	0.006	-0.001	0.004
	(-0.74)	(0.42)	(0.45)	(0.59)	(-0.20)	(0.41)
Number of Business Segments	0.0004	0.0004	0.0003	0.0006	0.0003	0.0006
	(1.54)	(1.56)	(1.53)	(1.59)	(1.52)	(1.60)
Departing CEO Stock Ownership	-0.0035	-0.0024	-0.0066	-0.0012	-0.0051	-0.0040
	(-1.23)	(-1.17)	(-1.35)	(-1.15)	(-1.26)	(-1.24)
Managerial Entrenchment	0.054**					0.041*
Component	(2.16)					(1.79)
Monitoring Component		-0.044**				-0.040**
(Institutional Ownership)		(-1.98)				(-2.00)
Monitoring Component			-0.031*			-0.023*
(Board Ownership)			(-1.77)			(-1.71)
Post-Retirement				0.072		0.055
Career Component				(1.58)		(1.52)
Incoming CEO Component					-0.010*	0.009*
					(-1.83)	(-1.80)
R^2	0.03	0.04	0.03	0.02	0.04	0.06
N	183	183	183	183	183	183

The managerial entrenchment component has a significantly positive effect on the level of managerial conformism. On the other hand, monitoring components have significantly negative effects. If the incentives of the incoming CEO are aligned with those of the shareholders, managerial conformism is significantly lower. The only interesting difference in stock performance results is that post-retirement opportunities have no significant effect on the level of managerial conformism, measured by the

change in stock performance at the end of the probationary period. Again, similar to the findings presented in the previous tables, the incentives of the incoming CEO have significant effects on the level of managerial conformism, while the departing CEO's stock ownership remains insignificant.

Probably the most direct measure of the level of managerial conformism is the increase in the number of policy decision taken by the firm after the new CEO gets the combined title. Since most of the reputation of a manger lies on the decisions he implements, the departing CEO in the firm would have incentives to ensure the continuation of his policies, while the new CEO would have incentives to keep the status quo in order to curry favor. However, when the new CEO completes the probationary period and obtains the combined title, most of these incentives would disappear, leaving the new CEO free to implement his own policies. As stated in H_5 in chapter 3, if managerial conformism exists in the firm, then the number of major policy decisions undertaken is expected to increase significantly after the completion of the probationary period. The higher this increase, the more serious managerial conformism problems are in the company. Table 7.7 presents the results of regression analyses where the increase in the number of policy decision after the completion of the probationary period is used as the dependent variable.

Results indicate that, consistent with expectations and previous results, larger and older firms have lower degrees of managerial conformism. The increase in the number of major policy decisions is significantly lower for larger and older firms in all regression specifications. The share ownership of the departing CEO again has no significant effects of the level of managerial conformism.

Table 7.7
Determinants of the Change in Number of Policy Decisions
(Using the Principal Components Analysis Results)

The dependent variable in the regression models is the change in the number of policy decisions of the firm upon the conclusion of the probationary period when the new CEO takes on the combined CEO and Chairman of the Board title (i.e. Δ_C). Log size is the natural logarithm of the market value of the firm, and market-to-book is the ratio of the market value of the firm to its book value. Firm age is the number of years since the establishment of the company until the start of the probationary period. Managerial entrenchment, monitoring, post-retirement career and incoming CEO components are the five components with eigenvalues greater than one in the principal components analysis. The 20 firms with incomplete succession processes have been excluded from the regressions. All errors are White-corrected for heteroskedasticity and t-statistics are presented in parentheses. *, ** and *** represent significance at the 10%, 5% and 1% levels, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Intercept	1.14	1.17	1.35	1.26	1.16	1.08
	(0.93)	(0.95)	(1.12)	(1.07)	(0.95)	(0.79)
Log Size	-0.71*	-0.84**	-0.70*	-0.72*	-0.82**	-0.59*
	(-1.90)	(-2.01)	(-1.90)	(-1.94)	(-1.99)	(-1.77)
Firm Age	-1.05*	-1.04*	-1.02*	-1.03*	-1.04*	-1.03*
	(-1.90)	(-1.90)	(-1.75)	(-1.86)	(-1.90)	(-1.88)
Market-to-Book	0.02	0.03	0.04	0.05	0.03	0.05
	(1.42)	(1.48)	(1.50)	(1.54)	(1.52)	(1.56)
Number of Business Segments	1.07	1.03	1.02	1.06	1.03	1.02
	(1.53)	(1.44)	(1.40)	(1.50)	(1.43)	(1.41)
Departing CEO Stock Ownership	-1.002	-1.01	-1.007	-1.005	-1.00	-1.009
	(-0.98)	(-0.99)	(-0.94)	(-0.94)	(-0.92)	(-0.98)
Managerial Entrenchment	1.28***					1.20***
Component	(3.24)					(3.08)
Monitoring Component		-2.03***				-1.76***
(Institutional Ownership)		(-5.22)				(-3.61)
Monitoring Component			-1.07*			-0.99*
(Board Ownership)			(-1.86)			(-1.72)
Post-Retirement				0.97*		0.92*
Career Component				(1.70)		(1.69)
Incoming CEO Component					-2.41**	-2.18*
					(-2.03)	(-1.89)
R^2	0.13	0.16	0.10	0.09	0.12	0.27
N	183	183	183	183	183	183

Consistent with the findings in previous tables managerial entrenchment and the potential for future employment for the departing CEO exacerbate the level of managerial conformism, while outside and board monitoring alleviate it.

In all seven tables in the chapter the effect of departing CEO stock ownership is insignificant, while the stock ownership of the incoming CEO in the first two tables with all the proxies and the incoming CEO component in the later tables, reduce managerial

conformism. In other words, aligning the incoming CEOs incentives with those of the shareholders is a more effective control mechanism than aligning the incentives of the departing CEO. This may suggest that more of the managerial conformism comes from the incoming CEO's need to curry favor with the departing CEO and the board then the departing CEO enforcing his methods. It may also mean that by the time the departing CEO retires, his stock ownership provides less incentives than future possibilities do.

The results presented in all seven tables are consistent. Older and larger firms, firms and firms with stronger outside or board controls on management experience lower degrees of managerial conformism. However, the level of diversification in the firm and the growth potential do not seem to have significant effects on the level of managerial conformism. Entrenchment of the departing CEO, on the other hand, exacerbates the managerial conformism problem in probationary succession processes. Increasing the stock ownership of the incoming CEO seems to be a better solution to the managerial conformism problem than increasing the stock ownership of the departing CEO, since the latter has no significant effects on any of the measures used for the level of managerial conformism. Effective board and institutional owner monitoring seem to help alleviate managerial conformism problems significantly.

CHAPTER 8
CONCLUSION

I analyze the prevalent CEO succession process in US firms, termed 'passing the baton' in which the incumbent CEO/chairman of the board relinquishes the CEO title to his heir apparent but remains as chairman of the board for a probationary period to better monitor the new CEO and pass down any relevant information. At the end of this probationary period, the new CEO is awarded the combined title of CEO and chairman of the board if he is successful, or is terminated otherwise.

While the benefits of this succession system have been analyzed thoroughly in finance literature, the conflicts of interest between the former and the new CEOs inherent in this process due to the incentives of the incumbent CEO to ensure the continuation of his policies and visions for the firm as well as protecting his own performance from depreciating in value, have received little attention. The retiring CEO has promotional incentives of serving on other firms' boards based on his past performance, increasing his incentives to engage in succession-securing behavior.

The results indicate the existence of agency costs in the succession process due to this managerial conformism. Managerial entrenchment seems to exacerbate these problems, while the monitoring effectiveness of the Board of Directors and external monitoring mechanisms such as external Board members and institutional blockholders reduce these agency costs and the probability of managerial conformism.

This dissertation revisits the Alchian and Demsetz (1972) question of "who monitors the monitor?' and presents yet another source of conflicts within top management of the modern firm. Furthermore, these findings provide pivotal information on the contemporary debate of the separation of the CEO and chairman of

the board titles by showing that existing academic evidence is not conclusive. Additionally, with contemporary corporate events that have called to attention the effectiveness of both external and internal control mechanisms of firms, my results bear significant value.

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